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**INTERNET GAMBLING REGULATION**

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## **Internet Gambling Legislation**

### **EXECUTIVE SUMMARY:**

Up until roughly ten years ago the Internet had not yet gained a strong foothold on American culture. The Internet, as a tool used to work, research, or as a recreation device, was just beginning to make its transition from Southern California into home all over the United States and across the world. Breaking out of the once confusing and highly complicated mold that had enveloped its earlier years and into the homes and offices of nearly every American has led to an almost new uprising. People can now do nearly every function of their everyday life with the simple point and click of a mouse. The mundane tasks of scheduling vacations, ordering pizza's, and even grocery shopping has become something that can be done from within the homes and private spaces of any person with access to the ever growing Internet. However, the problem also exists that the same device that makes everyday tasks so easy, private, and available, can also make criminal activity just as easy, private and accessible.

It then must be examined that with something such as the Internet, with its all encompassing and widespread reach, can the state properly regulate the criminal problems or is it just too big?

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## **INTRODUCTION:**

### **A. General Background**

The legalities of gambling via the Internet offer a broad range of difficult problems as well as feasible alternatives. Questions of the Internet itself can often blur the bright line rules established for gambling as a separate legal entity. Much of the debate arises because of the large and over-encompassing range that the internet has. Not only must legislation establish rules that bind the user, but they must also discover where the server (or Internet “Bookie”) is located and bind the source of the gambling operation as well. This can create numerous problems which may force legislation to track the rules and laws of many states, nations, and even many continents.

It seems quite important to start with how the Internet is operated. The Internet is broken down into 4 distinct separate entities. The 1<sup>st</sup> entity is the corporation, or Internet provider, that formulates a product and uses the internet to sell or display the product. Next there are the servers. These are systems which develop web sites and provide the corporations product over the Internet. 3<sup>rd</sup>, there are Internet hosts (such as AOL, Netzero, Juno, etc.) which obtain Internet information, organize it, and allow users access to information provided by the servers. Lastly, there are the users which access the information provided by Internet hosts. The users gain access to the servers via their own personal home computers and retrieve information from the servers to buy or obtain the corporations products. Herein lies the problem. These 3 entities can be continents apart and can work almost in unison to transfer a product to the end user. Many times laws in one country do not coincide with laws in another. So when a corporation selling a product in Asia wishes to sell that product to a person in the United States the same laws

will not apply to both entities. This can create interstate conflicts since many states have different laws and rules regarding specific issues. States such as New Jersey and Nevada have less stringent gambling laws and can now promote their gambling operations around the world because of the freedom that the internet allows them. So who should be regulated and controlled; the corporations, the servers, or the end users? And how should they be regulated?

### **1. Kansas gaming laws**

Kansas has already begun implementing laws that bind Internet gambling within the state; however, the laws that have been established only place restrictions on the gambling done from computers within the state of Kansas. These laws do not regulate internet gambling as a whole. In fact, as the law is written, it is only a “partial” crime to computer gamble within the state. “Partial” means that the way the law is written, only the end user is punished, instead of both the user and the provider. The law states that the person gambling over the internet is subject to prosecution but does not establish boundaries for participants out of the state who may be controlling the operation or gambling with the Kansas citizen.

KSA § 74-9808 examines Kansas gaming laws. This section explores the different illegal activities involved with gambling within or on Indian reservations. The statute categorizes felony and misdemeanor offenses relating to illegal gambling activities. Many of the prohibited acts in the statute involve underage gambling on tribal reservations. Since many Internet gamblers can easily conceal their ages and identities it would make it difficult for the state to control and enforce Internet gambling under current Kansas gaming laws. Also, much of the statute imposes penalties upon those

individuals who cheat while gambling upon tribal reservations. Internet gambling, run through the Indian reservations, would do 2 things: 1) it may make it easier to cheat while gambling, or 2) it could possibly make it more difficult to do so. Depending on the level of computer expertise the individual has, cheating could become easier and could open the door for Indian gambling operations to be taken advantage of.

## **2. Federal law**

What online gambling laws are currently in use? There are several federal laws which work to control gambling in the United States. The Federal Interstate Wire Act established in 1961 and codified as 18 U.S.C. §§ 1084 (1994) was established to assist various states in the enforcement of their laws pertaining to gambling by prohibiting the use of wire communication facilities which are used for the transmission of bets or wagers. Also, 1961 U.S.C.C.A.N. 2631 suggests that it is an unlawful activity for anyone engaged in the business of betting or wagering knowingly to use a wire communication facility for the transmission of bets or wagers. On the same day that Congress passed the Wire Act above, it also passed the Travel Act, codified as 18 U.S.C. §§ 1952. This act prohibits travel or using “any facility in interstate or foreign commerce, with intent...to promote, manage, establish or carry on, or facilitate the promotion, management, establishment, or carrying on, of any unlawful activity.” This act also defines unlawful activity as “any business enterprise involving gambling.” Lastly, the Organized Crime Control Act of 1970, codified as 18 U.S.C. §§ 1955 (1994), prohibits conducting, managing, or financing a gambling business involving 5 or more persons.

The third question that legislators should pose is “Is online gambling Illegal?” Many state laws do not specifically answer this question; it has normally been left open

for federal debate. Federally there are 5 Acts and statutes that challenge and discuss the legality of online gambling. They are the Wire Wager Act, the Travel Act, the Interstate Transportation of Wagering Paraphernalia Act, the Professional and Amateur Sports Protection Act, and the Federal Aiding and Abetting Statute. These five areas attempt to regulate online gambling, however, there are many inconsistencies between these acts and state enforcement objectives.

### **B. Policy objectives**

In order to fully examine the issues surrounding Internet gambling the legislation must ask several questions. First, “should internet gambling be regulated?” Many pro-gambling organizations argue “why regulate it at all?” Is gambling a victimless crime and does it need the strict scrutinization of state and federal legislative acts. Based on these two conflicting questions it is important to further examine some of the elements that underlie gambling. These can involve addiction, morality, fraud, and lost revenue. Overall, the concern of Internet gambling offers many viewpoints and opposing parties can often find traceable flaws in any argument opposing their own.

#### **1. Preventing fraud and other abuses**

Fraud committed by Internet gambling is potentially much greater upon the player than upon the Internet gambling establishment. Often, after receiving deposits from players, an Internet casino could abscond with the funds or effuse to pay a player the winnings. (Comment, Bib. D.1.) Since the design of online casinos allows unscrupulous operators to close down their businesses and disappear practically instantaneously, players could find it difficult to retrieve their money. In addition, gamblers cannot be

certain that online casinos operate their games fairly and the potential for fraud in the realm of online gambling is a valid concern. (Comment, Bib. D.1.)

## **2. Combating the adverse social effects of gambling**

In terms of the social costs of gambling, there are two focal areas; 1) the adverse social costs of gambling on corporations defrauded by gambling employees, and 2) the adverse social effects of gambling on the gambler. Both of these can create a paramount of problems that can lead to adverse social effects such as theft, fraud, deceit, and emotional, physical and familial problems. The states ultimate objectives are to create a safe, peaceful environment for its citizens without violating any of the rights afforded to them under the Constitution of the United States.

## **3. Capturing revenue for the state**

Internet gambling has the potential of becoming a tremendous source of revenue for the state. One estimate predicts that Internet gambling could produce as much as ten billion dollars in revenue from the United States alone. (Comment, Bib. E.1.) States that have legalized gambling collect significant taxes from these gambling operations. For example, Nevada's gambling and hospitality industry generates in excess of \$2 billion annually in state, local and federal taxes, and the New Jersey gambling industry paid \$303.2 million in revenue taxes in 1996. (Comment, Bib. E.2.) Internet casinos allow gamblers to patronize gambling establishments that are not licensed by any state. States, therefore, will obtain no tax revenues from online casinos that are either unlicensed or licensed by other jurisdictions. States could see a significant decline in tax revenues if gamblers reduced their patronage of state-licensed gambling establishments for their online counterparts. (Comment, Bib. E.2.)

#### **4. Maximizing individual freedom of choice**

The conflict between pro-gambling organizations and anti-gambling activists is one that is not likely to end soon. Opponents to legalized gambling argue that gambling cuts away at our nations Constitution because freedom of choice to decide to gamble is taken away by the compulsion to gamble. However, pro-gambling organizations argue quite the opposite. They argue that the freedom to gamble is one that is inherent in the constitution and must be preserved. In an issue such as this the state must recognize the right and necessity for the state to limit freedom when its exercise harms other people, infringes upon their rights, or offends accepted moral principles as well as recognize that the rights of the citizens often outweigh or conflict with the states power to eliminate harmful activities.

#### **5. Limiting enforcement costs**

The cost to the state in tax dollars to enforce many gambling laws is a great one. Many different organizations are involved in tracking and convicting individuals involved in such activities. Often times the state must coordinate the efforts of peace officers, law enforcement officers, and law enforcement agencies within the state in order to enforce and properly prosecute violators. In addition, many states require that law enforcement agencies, who investigate such matters, must report to the state enforcement commission all violations. This can create an enormous amount of man hours worked and tax dollars spent.

Aside from enforcing laws and the costs associated with do so, there are also many costs associated with prosecuting offenders. As stated in the article *The Internet Gambling Fallacy Craps Out* by Joel Michael Schwartz, “many state and federal law

enforcement agencies currently wrestle with the difficulty of prosecuting crime that utilizes a borderless and boundless medium such as the Internet.” (Comment, Bib. E.3.)

### **C. Policy alternatives**

Overall, the range of policy alternatives will be sharply limited due to federal preemption and the dormant commerce clause which will be discussed in the Implementation section. The scope of state regulatory authority is limited but within that scope the following policy alternatives are provided.

#### **1. Further study; wait to take action until something further emerges**

One possible policy alternative, which many states have, is to simply monitor, study and wait to take action until something further in the field of Internet law emerges. The Internet, as a legal entity, is changing so rapidly that many case law decisions regarding Internet law are already out of date before they are even published. Useable, workable, applicable laws are unable to take hold quickly enough for them to be effective. This may force the legislature to simply wait until there is either a slowing down of technological change (which is not likely to happen anytime soon) or either wait until other states develop applicable law to deal with the Internet criminal problems.

#### **2. Clarify and strengthen the sanctions on Internet gamblers**

Kansas laws establish sanctions and penalties on gamblers and gambling operations within the state of Kansas. KSA sections 21-4303, 21-4304, and 21-4305 impose sanctions on gamblers and commercial gambling operations but they do not provide strict sanction on violators. The penalties involved merely act as a mild deterrent imposing penalties ranging from minimal jail time to fines. In order to strongly deter gambling activity within the state legislators would have to stiffen the penalties imposed

on those who participate in such illegal activities. The penalties and fines would have to be such that would-be gamblers would not wish to risk the activity in order for the thrill of gambling.

### **3. Legalizing and taxing Internet gambling**

One possible way to avoid the troublesome project of illegalizing Internet gambling is to simply legalize it and properly tax it. The state always has the opportunity to pass legislation that would make it a crime to be involved in offering Internet gambling opportunities. The state could pass laws, and make the laws known to the people of the state; however they would also have to recognize that members involved in illegal Internet gambling activities would not be easily prosecuted. The difficulties involved in capturing and tracking illegal activity on the Internet is much too difficult to make it a feasible objective of the state to prosecute and convict a majority of the offenders.

### **4. Lobby for implementation of HR 2143**

The National Gambling Impact Study Commission in 1999 recommended the passage of legislation to prohibit wire transfers to Internet gambling sites of the banks which represent them. (H.R. 2143, Bib. B.1.) This bill is known as H.R. 2143. The effectiveness of H.R. 2143 may be one of the few ways that the state can properly regulate Internet gambling. The bill acts as a way to stop credit card transactions between Internet gamblers and the corporations who control them. Regulation of creditors, credit card issuers, financial institutions, operators of terminals at which as electronic fund transfers may be initiated, money transmitting businesses, international, national, regional, or local networks utilized to effect a credit transaction, electronic fund transfers, money transmitting service, or a participant in such network would all be

covered and regulated under this current bill. H.R. 2143 also implicates what organizations would regulate and enforce this new legislation as well as specifically designates restricted transactions.

## **5. Regulate Internet Service Providers**

A possible policy alternative for the state may be to regulate Internet service providers. This could be done much like HR 2143, only on a state level and much smaller scale. Sanctions could be administered upon ISP's if they allowed online gambling operations to be conducted through their servers. Internet service providers could be monitored and fined if they were to violate the regulations and online gambling sites could possibly be regulated effectively with minimal discourse.

### **ANALYSIS:**

#### **A. Analyzing Potential Barriers**

##### **1. Is Internet Gambling exempt from current law and hard to reach or regulate?**

Many current laws create conflict between the law and the imposition of the law upon Internet gambling. This can make it hard to regulate Internet gambling as a whole. Most Internet gambling defendant corporations locate overseas, and without the power of extradition, there is no effective manner in which authorities can enforce the laws of the United States. Department of Justice officials wrote in an analysis last year that "since some form of gambling is legal in virtually every state our ability to persuade a foreign country that gambling must be vigorously combated is diminished."

Since it appears that the enforcement of laws against operators of Internet gambling is highly impractical, states must instead focus their efforts upon the reception of the Web site instead of upon its transmission. There are 2 options for regulators to

focus their attention upon; 1) they could prosecute the individual gambler, or 2) regulators could force Internet service providers to block access to Internet gambling sites. Providers could avoid prosecution by simply blocking Internet gambling Web sites. These may be only a few of the ways in which Internet gambling could properly be regulated.

## **2. Jurisdictional Limitations and the Dormant Commerce Clause**

Jurisdictional problems may arise when dealing with how to regulate Internet gambling operations who remain based over seas. This forms one of the single largest obstacles regulators must face. KSA 21-3104 establishes the criminal jurisdiction of this state as: 1) a person who commits a crime wholly or partly within this state, 2) being outside the state, he counsels, aids, abets, or conspires with another to commit a crime within this state, or 3) being outside the state, he commits an act which constitutes an attempt to commit a crime within this state. In a Kansas Attorney General opinion, Carla Stovall states “if a bet is placed or a lottery is entered into via a computer located in the state of Kansas, then the crime is committed partly within this state and participants in the crime may be prosecuted in this state.” (Attorney Generals Opinion, Bib. C.1.)

Two forms of jurisdiction exist under current US law: subject matter jurisdiction and personal jurisdiction. In order to exercise jurisdiction over a foreign defendant the United States must have both personal and subject matter jurisdiction. Subject matter jurisdiction is not an essential issue for the state legislature because it deals primarily with matters involving the United States as a whole and not just individual states; however, personal jurisdiction may become a prevalent matter.

Under personal jurisdiction there is also another two-pronged test that must be satisfied in order to obtain jurisdiction over a foreign defendant. This test focuses upon the nature and quality of the defendant's contact with the forum, and the sufficiency of these contacts. If a foreign Internet gambling organization developed a large number of members in one particular state, then the personal jurisdiction requirement may possibly be met. If a suit was raised from the contacts the defendant had in the forum state, then jurisdiction would be met because the defendant's contact with the state (the customer's activity with the company) would be the basis for the criminal claim against them.

Jurisdiction may meet all the required criteria for prosecution within the United States, but if other countries will not cooperate then regulation will fail. For example, despite the fact that the U.S. has placed laws upon Internet gambling activity, some countries are using it as a way to boost their local economy and are embracing it. Unless there is some uniform policy against gambling among the different countries, there will always be gambling sites on the Internet. Thus, in order to properly regulate Internet gambling, the United States must endeavor to establish an international policy regarding gambling on the Internet. (Comment, Bib. C.2.)

The Dormant Commerce Clause also poses potential regulation problems. The Dormant Commerce Clause in effect allows states the ability to regulate their own interstate commerce. Since gambling can be considered a form of interstate commerce the federal laws created and the state regulatory efforts may conflict.

## **B. Alternative Effect on Policy Objectives**

### **1. Combating the adverse social effects of gambling**

A recent study by the Australian Institute of Criminology (AIC) and accountancy firm PricewaterhouseCoopers found that fraud, committed to sustain a serious gambling habit, resulted in an average loss of \$218,000. (Article, Bib. D.2.) In fact, the study showed that most gamblers who committed fraud were employed at the time of their offenses and nearly half of offenses were committed against employers. (Article, Bib. D.2.) The study also showed that two-thirds of offenders went to jail for periods ranging from 3 months to 6 years. The report indicated that problems gamblers did not receive much sympathy from the judge and in no case was gambling accepted by the judge as a mitigating factor in reducing sentences. (Article, Bib. D.2.)

There are three main reasons for the increasing problem of compulsive, problem, pathological gamblers. One is that the social attitudes towards gambling have changed from being negative to positive. Another reason is that gambling is accessible to everyone not only through existing legalized forms, but also through the Internet. The last reason for excessive gambling is that the number of people living in emotionally and financially stressed families is growing. (Article, Bib. D.3.)

One main issue, and probably the one most talked about, is the effects of gambling on the economy. Right now, Americans are spending more on various types of gambling than on theme parks, video games, spectator sports, and movie tickets combined. As Donald Trump put it, "People will spend a tremendous amount of money in casinos, money that they would normally spend on buying a new refrigerator or a new car." Local businesses will suffer because they'll lose customer dollars to the casinos."

This could be applied to lotteries, bets, and other forms of gambling. For every dollar the state receives in gambling revenues, it pays nearly three dollars because of economic and social costs of gambling such as an increase in criminal justice and social welfare. Each problem gambler costs the government and private economy at least \$13,200 a year. Expanding gambling would be more costly than an additional hurricane Andrew every year (32 billion dollars in damage). (Article, Bib. D.3.)

Most pro-gambling people say that legalized gambling helps the economy, but according to statistical data they are wrong. For example Utah, a state with no legalized gambling, has the healthiest growing economy in the nation. Also, businesses prefer locating in gambling-free states because there are lower taxes and there are better community and business environments. To help the tremendous gambling problem in the U.S, the Gambling Impact Study Commission has already issued recommendations to congress. Some include a ban on wagering on college and amateur events, a ban on Internet gambling, and a ban on credit-card cash-advance machines in gambling parlors. The commission suggests raising the legal age for wagering to twenty-one, and taxing gambling revenues to pay for programs to treat problem gamblers. It also wants restrictions on political contributions for people operating or planning to operate gambling facilities. The commission (1999) looks down on existing research on gambling calling it “flawed by insufficient data, poor or underdeveloped methodology, or researchers’ biases”. They also scorned at the attachment of money figures to some of the social problems caused by pathological gamblers saying, “How can one calculate the ‘cost’ of the two children that died while locked in cars as their parents or caretakers gambled in nearby casinos?” People who support gambling do not have enough evidence

to prove that it is good compared to all the problems that come along with it. (Article, Bib. D.3.)

## **2. Maximizing individual freedom of choice**

Many pro-gambling organizations argue that gambling is an exercise of free choice and to legalize it is a violation of their Constitutional rights. They believe that instead of an outright ban on Internet gambling; why not simply regulate online play? These groups make a direct correlation between gambling regulation and alcohol prohibition. They state “Late last year, Time Magazine published its list of the 100 Dumbest Ideas of the 20th Century - unsurprisingly, alcohol prohibition was selected as the single dumbest idea. George Santayana warned us that those who do not learn from history are doomed to repeat it. We can only hope that the prohibitionists in Congress find themselves reading about the 1920's sometime soon.” (Article, Bib. D.4.)

Adversely, anti-gambling organizations expel the notions of free choice. They state that “compulsive gambling is not an exercise of free choice. Addicted gamblers gamble out of a compulsion which they are unable to control. Organizations which depend on gambling as a source of funding increasingly feel they have no choice. Finally, there are business people whose personal values may be against gambling; yet they feel they have no choice but to support gambling in the community and perhaps within their own business in order to survive. So as I hear it, when it comes to gambling, freedom of choice seems decidedly absent.” (Article, Bib. D.5.)

These organizations who expel gambling as a moral and societal wrong also state “Addiction is a loss of freedom. Many people have worked hard to build a foundation for freedom in our country and many have made the ultimate sacrifice for that freedom.

Upholding and preserving our freedom is a sacred trust; and allowing ourselves as a society to become increasingly addicted to gambling betrays that trust.” (Article, Bib. D.5.)

It is said that a good society will do 3 things: (1) it will protect and promote the welfare of all its citizens. (2) It will provide a range of freedom for individuals as extensive as possible compatible with equal freedom for all other persons. (3) It will provide rights, opportunities, protections and rewards to all on an equal basis and will not discriminate against any person on irrelevant grounds. (Comment, Bib. D.6.) These are principles that many would accept, however, there is inevitably a tension that can arise between individual freedom and the right of the state to limit freedom for moral and social reasons.

Initially, it seems wise and just to give individuals as much freedom as possible to do as they please, consistent with an equal freedom for everybody else. But we also recognize the right and necessity for the state to limit freedom when its exercise harms other people, infringes upon their rights, or offends accepted moral principles. (Comment, Bib. D.6.)

### **C. Alternative Analysis**

#### **1. Further study; wait to take action until something further emerges**

Waiting to take action on a specific issue may seem difficult or inconceivable, however, often times it is a necessary task. As mentioned, the Internet is a highly evolving and ever changing entity. This makes it extremely difficult to properly regulate all illegal activities that occur in the realm of cyberspace. Many laws implemented, including case laws, are obsolete before they are even printed. Because of this, it may be

necessary to monitor and study the regulations created by other states for the time being and wait until further change occurs either within the state, other states, or the federal government. This could be an “active waiting” period in which the state watches other state carefully for a feasible approach to the problem of Internet regulation. During the time that the state takes to wait, watch, and listen, the rapid advancements in technology may pose the answer and may make Internet regulation possible.

State laws currently exist that provide penalties and sanction on Internet gamblers within the state of Kansas. These laws appear adequate for the time being to control the illegal gambling within the state. The laws are based around punishing the gambler and commercial gambling operations; they are not based upon the premise of punishing Internet gambling casinos. This may be a problem, but one that may have to wait for the time being.

## **2. Clarify and strengthen the sanctions on Internet gamblers**

Many current laws make it a crime for people in the state of Kansas to conduct or participate in any type of gambling including Internet gambling. In order to understand fully the levels and severity of the sanctions involved the categories must be broken down into 3 sections. First, what defines gambling in the state of Kansas? Next, what are the penalties for independent gamblers and commercial gambling operations within the state? And finally, what are the sanctions imposed upon those who use their premises for commercial gambling?

Gambling is defined in KSA 21-4303 as (a) making a bet; or (b) entering or remaining in a gambling place with intent to make a bet, to participate in a lottery, or to play a gambling device. (Kansas Statutes Annotated, Bib. A.1.) Gambling, according to

this statute is a class B nonperson misdemeanor. Class B misdemeanors, examined in KSA 21-4503a, impose a fine upon the violator for a sum not to exceed \$1000. (Kansas Statutes Annotated, Bib. A.2.) Jail time may be assessed but in the case of a misdemeanor is usually not extensive, if at all.

Commercial gambling imposes a few more stringent sanctions upon offenders. KSA 21-4304 defines commercial gambling as (a) operating or receiving all or part of the earnings of a gambling place; (b) receiving, recording, or forwarding bets or offers to bet or, with intent to receive, record, or forward bets or offers to bet, possessing facilities to do so; (c) conducting a lottery, or with intent to conduct a lottery possessing facilities to do so; or (d) setting up for use or collecting the proceeds of any gambling device.

Commercial gambling is noted as a severity level 8, nonperson felony. (Kansas Statutes Annotated, Bib. A.3.) “Gambling device” as listed in section “d” of this statute may constitute a computer and encompass Internet gambling. KSA 21-4503a lists the sanctions for a severity level 8 felony as possible imprisonment accompanied with a fine of no more than \$100,000. (Kansas Statutes Annotated, Bib. A.2.)

Lastly, KSA 21-4305 supplies sanctions for individuals who permit their premises to be used for commercial gambling. This statute states that granting the use or allowing the continued use of a place as a gambling place, and permitting another to set up a gambling device for use in a place under the offenders control are both class B nonperson misdemeanor offenses. (Kansas Statute Annotated, Bib. A.4.) Again this statute would allow for a possible imprisonment period followed by a fine of no more than \$1000. (Kansas Statutes Annotated, Bib. A.2.)

In order to properly deter unwanted criminal activity the penalties for a crime must injure the offender. Much of the Internet gambling that takes place in the state of Kansas would properly fit under the gambling statute KSA 21-4303; some may even fit under KSA 21-4305. These do not require strict penalties and likely would not deter a would-be offender. KSA 21-4304 imposes the strictest penalties; however this statute would likely apply to the operator of the gambling operation. Applied to Internet gambling, the operator of a gambling operation would most likely not be in the state of Kansas and may not even be present within the country. In order for the state to properly regulate Internet gambling within the state of Kansas, KSA 21-4305 and 21-4303 would have to be strengthened to impose stricter penalties for violators of these statutes.

The laws as written do not specifically control Internet gambling, they merely police gambling as a whole. The far reaching arm of the Internet provides for a much more complicated means of gambling within the state. Many state residents could gamble and suffer penalties, while Internet casinos operating off shore could remain undeterred. Laws would have to be written as such that they would control the Internet gamblers and Internet gambling operators as well. This poses the largest problem for the state legislators. They must find adequate ways to control both entities and enforce and regulate the laws that they impose as well.

Enforcement efforts, due to the long distance abilities of the Internet, would have to be a joint effort that would require the use of state and federal enforcement agencies, as well as enforcement agencies based outside the United States. Since many foreign countries rely on legal Internet gambling as a source of revenue this may be a difficult

task. Likewise, jurisdiction to enforce these overseas entities would be a factor to consider as well.

### **3. Legalizing and taxing Internet gambling**

Another possible alternative for the state is to legalize and tax Internet gambling. Tax revenues from gambling as a whole would create large profits for the state. However, as mentioned earlier, many states without legalized gambling have a much stronger economy than those states with legalized gambling. The conflict of interest in an alternative such as this would arise based primarily upon the fact that revenue could be gained and countered with the idea that the economy may be stringer without it.

Enforcement of an implementation such as this would primarily fall upon the state. Tax procedures would have to be written that would tax the individual gambler and the corporate gambling operation as well. Agreements could be made between federal tax enforcement agencies and state tax agencies to work collaboratively to tax Internet gambling winnings. As H.R. 2143 would restrict and monitor gambling activities in order to eliminate them, this method would monitor gambling activities in order to simply tax them. State agencies could monitor legalized Internet gambling by monitoring credit transactions and wire transfers and tax individuals based upon their earnings or spending.

### **4. Lobby for implementation of HR 2143**

H.R. 2143 is an act proposed to Congress to prevent the use of certain bank instruments for unlawful Internet gambling and for other purposes. Since Internet gambling is primarily funded through personal use of bank instruments, including credit card and wire transfers, regulation of the entities would be a possible intermediary between the gambler and the Internet gambling casino. This bill states that “Internet

gambling conducted through off-shore jurisdictions has been identified by United States law enforcement officials as a significant money laundering vulnerability.” (H.R. 2143, Bib. C.3.) H.R. 2143 would regulate Internet gambling by forcing designated payment systems to establish policies and procedures that would identify and prevent restricted transactions. This would be accomplished by either blocking the transaction entirely or provide that any person involved in any restricted transaction to identify the transaction by a means of codes or authorized message.

Enforcement of H.R. 2143 would be carried out by the cooperated efforts of the Federal functional regulators and the Federal Trade Commission (FTC) under applicable law in the manner provided in section 505(a) of the Gramm-Leach-Bliley Act. (H.R. 2143, Bib. C.3.) The enforcement of this act would rest almost entirely upon the federal system and leave little involvement on the state level. Certain areas would be considered and factored by the FTC when regulating Internet gambling operations: 1) the extent to which a person is extending credit or transmitting funds knowing the transaction is in connection with unlawful Internet gambling, 2) the history of the person extending the credit or transmitting funds, 3) the extent to which the person is maintaining policies in compliance with regulations prescribed, 4) the feasibility that any specific remedy prescribed can be implemented by such person without substantial deviation from normal business practice, and 5) the costs and burdens the specific remedy will have on such person. (H.R. 2143, Bib. C.3.)

H.R. 2143 may be the most effective way for Kansas to regulate Internet gambling. Despite the fact that many Kansas laws only regulate the gamblers, H.R. 2143 acts as a way to marginally regulate the gambling provider as well. As a intermediary to

Internet gambling operations and their customers, financial institutions and credit card companies would be the best possible regulated entity. Gamblers, and Gambling providers, rely upon their financial institutions to conduct the business of Internet gambling. No other possible medium exist for them transact business. The regulation of these entities would solely rely upon the legislature to pass this bill within the state of Kansas.

The benefits of H.R. 2143 is that it allows the state of Kansas to actually “do something,” as opposed to “doing nothing” as one policy alternative suggests. This allows Kansas and the federal government to be proactive in the enforcement of Internet gambling laws. For many conservative constituents, H.R. 2143 also allows the state to decide whether they wish to entertain the idea of gambling within the state or not. They would essentially have the option to either implement H.R. 2143 and eliminate Internet gambling within the state, or legalize Internet gambling and tax its profits. Variations on both could be useful as well. Lastly, H.R. 2143 does not clarify and strengthen the sanctions imposed on Internet gamblers. In fact, the act does not even mention the sanctions or penalties that would be assessed for individuals failing to abide by the act. The act itself, and how the act will regulate Internet gambling transactions is discussed, but the penalties for violating the act are non-existent.

### **5. Regulate Internet Service Providers**

In much the same way that HR 2143 regulates wire transfers and credit card corporations for allowing Internet gambling to be conducted through their services, the state could establish regulations upon Internet service providers that would regulate their activities. The state could create regulation that would monitor all activity that was being

conducted through ISP's, essentially quashing the ability of Internet gambling operations or gamblers to transact business.

Several problems arise when discussion of regulating ISP's and their information. The first potential problem arises at the heart of our nations Constitution. This nation was founded upon the premise that information be shared and transferred freely and openly. All US citizens should be able to have access to all information and a regulation of ISP's and the information and services they transfer could be a problematic area. Next, many Internet service providers have the ability to choose whether or not they conduct business in Kansas. If the state were to suddenly restrict their business they could essentially close up shop and take their business elsewhere. Regulation of such a free moving entity such as the Internet and their service providers may be a difficult task to embark upon.

In order for the state to adopt such laws it would be essential that new agencies be developed to monitor the activities of the ISP's. This in itself would become a monstrous affair. The amount of information that is transacted and processed through the Internet on a daily basis is astronomical. Creating an agency that could keep up with the large volume of Internet activity conducted daily would involve a great amount of effort and numerous resources such as time, money, and manpower.

## **LEGISLATIVE IMPLEMENTATION:**

### **A. MEANS OF IMPLEMENTING OBJECTIVES AND ALTERNATIVES**

In order to implement the objectives listed above the state would need to take the proper steps, or in some instances, take no steps. With the onset of ever changing laws involving cyberspace, the state may be well advised to monitor and study the Internet

regulation efforts of other states until further federal laws arise that would assist the state in proper regulating methods. This alternative would not involve changing any laws the state currently has.

In order for the state to clarify and strengthen sanctions on Internet gamblers current Kansas gambling laws would need to be altered. The imposition of penalties imposed under KSA 21-4303 and KSA 21-4305 would need to be heightened. Currently these statutes carry a fine of \$1000 and list the gambling offense as a class B misdemeanor. Misdemeanor offenses often carry minimal, if any, jail time. Simply put, violators of these 2 statutes would not face strict consequences. In order for these to be effective deterrence methods the legislature would need to raise the penalties involved in these statutes to felony offenses carrying higher fines and mandatory prison time. KSA 21-4304 carries the highest penalties for offenders. This statute is listed as a severity level 8 felony of which jail time is imposed and fines are higher. However, as will be covered below, this statute could easily be bypassed by running commercial gambling operations on federal Indian sovereign lands.

The next alternative would possibly require the state to create an agency that could properly regulate Internet gambling operations. By legalizing and taxing Internet gambling, the state potentially has strong means of usable revenue that could be collected from the Internet operations. However, to do so would require the state to form some group that would control the taxing of such entities. An agency that could have the power to regulate, with use of police power, as well as could collect revenue, would be the ideal form of controlling agency. In order to enact this alternative, the state would

have to eliminate KSA statutes 21-4303, 21-4304, and 21-4305. These statutes would directly conflict with legalizing gambling operations within the state.

Lastly, HR 2143 is a strong possible state alternative that could be utilized. In order to implement this bill the state would need to defer action for the time being, as discussed earlier, and wait until this bill was passed. This federal bill, if adopted by the state, could potentially control Internet gambling by regulating credit card transactions and wire transfers between Internet gamblers and the entities who run them. HR 2143 is a federal bill, which means that the state would need to take few steps in order to implement it within our state. The enforcement of HR 2143 would be carried out largely by federal agencies such as the FTC (Federal Trade Commission), this simply means that no new agencies would need to be created by the state in order to adopt this alternative.

**B. LEGAL CONSTRAINTS, Limits to legislators discretion, 2 main limits:**

Limitations of the state require focusing on 3 main questions; 1) What can the state do, 2) What cannot be done by the state, and 3) Where are the gray areas? As discussed previously, the state may be able to do several things, however, for the regulation to be effective it must implement and rely upon the help of federal action. Many of the policy alternatives rely on implementation of federal mandates. Because of jurisdictional limitations, bills such as H.R. 2143 need to pass in order for the state to regulate according to its limitations.

Several things that the state may not be able to do include obtaining jurisdiction over off-shore Internet gambling hosts or regulating Internet gambling operations on Tribal lands. Since many Internet gambling operations are developed and run in foreign countries, with the support of their local government, individual states may not be able to

properly regulate their activities. Likewise, many Internet gambling operations have now chosen to run their operations under the cover of Indian tribal laws. These tribal laws allow gambling within the Native sovereign lands which may make it difficult for the state to obtain jurisdiction over these organizations.

Lastly, several gray areas exist. For example, will the state legislature be willing to regulate and eliminate an entity that has the ability to capture revenue for the state, and if they wish to regulate Internet gambling whom will they enlist to lead the charge? By taxing Internet gambling operations the state could potentially obtain a great amount of revenue from the operation itself. Also, will the state be willing to regulate Internet gambling if federal law will preempt the implementation of state laws? Several Congressional committees have focused attention on the regulation of Cyberspace crimes. One such plan proposes to place the Securities and Exchange Commission (SEC) in charge of a committee to conduct professional computer security audits. This committee would control and be in charge of regulating all Internet activities, including criminal activities. However, opponents to the bill are concerned that the SEC may not be the “appropriate oversight body for a proposal that deals with computer security.” (Congressman, Bib. D. 7.)

### **1. Federal preemption**

There is always a threat that the federal government can preempt laws enacted by the state. One such problem arises when dealing with Native American tribe Casinos. These Native lands, which were largely established through treaties with the federal government, retain sovereign rights within their federally approved tribal lands. The federal government gives these tribes almost absolute rights to adopt their own laws, as

well as the individual power to enforce those laws. In many cases the federal government cannot even intervene, which means that the state would not be able to intervene as well. Thus, laws created by the state would be preempted by many laws passed from the federal government onto the Native American government.

**a. Native American Tribe Casinos (Supremacy Clause)**

In the 1980's, the federal government passed the Indian Regulatory Gambling Act, which brought casino gambling to many more states. (Comment, Bib. F.1.) This Act, which is codified as 25 U.S.C. § 2710, states in general "Indian reservations can conduct gambling operations if the state where they are located permits certain types of gambling." (25 U.S.C. 2710(b)(1), Bib. F.2.) This has opened the door to many gambling operations throughout the US, and even more specifically, throughout the Midwest.

In order to secure regulation of gambling as a whole the National Gambling Impact Study Commission (NGISC) made a series of decisions on the local and state governmental levels. These decisions led the Commission to believe that its efforts to regulate Internet Gambling would be better addressed by the federal legislation. In fact, the National Gambling Impact Study Commission recommended that states are best suited to regulate gambling in all but two areas: Internet gambling and tribal gambling. (Comment, Bib. F.3.)

Several attempts were made under the Internet Gambling Prohibition Acts of 1997 and 1999 (also known as the Kyl Bill after Senator Jon Kyl) to regulate Internet and Indian gambling as a whole by placing strict restrictions on individuals involved in these activities. These Acts involved 3 levels of enforcement which included fines, imprisonment, and a mandated elimination of a particular Internet gambling site.

(Comment, Bib. F.3.) Several exemptions were allowed under the 1997 Kyl bill which included exemptions for horse racing and fantasy sports only where “winners receive a prize if such participation is without charge to the participant or any charge is limited to a reasonable administrative fee.” (Comment, Bib. F.3.) Groups that were displeased with the 1997 Kyl bill included Native Americans and Internet service providers (“ISPs”). Native American tribes were unable to gain an exemption for Internet lotteries and ISPs were angered because the bill would have allowed federal authorities to terminate customer accounts that had participated in Internet gambling. (Comment, Bib. F.3.) However, despite the fact that the House Subcommittee on crime approved the bill, due to a shortage of time the bill was never voted on and was never passed by Congress.

Gambling on Indian reservations continued and the foundation they were formed upon came from a Supreme Court decision in the case of *California v. Cabazon*. This case introduced what was to be known as the Indian Gaming Regulatory Act (IGRA). An article in the *Federal Communications Law Journal* discusses the decision in detail:

Large scale gambling on Indian reservations traces its origins to a landmark 1987 Supreme Court decision. “In *California v. Cabazon Band of Mission Indians*, the Supreme Court upheld the right of tribes as sovereign nations to conduct gaming on Indian lands. The Court ruled that states had no authority to regulate gaming on Indian lands, if gaming is permitted for any other purpose.” As a result of the favorable Supreme Court ruling, Congress passed the IGRA in 1988, recognizing Indian gaming rights. The IGRA faced heavy opposition from large casino cities, specifically Las Vegas and Atlantic City. Conversely, states supported the IGRA as a means of establishing minimal control over tribal gaming. In the end, the IGRA “was a political compromise that pleased neither the states nor the tribes.”

The IGRA divided gaming into three classes. Class I gaming, which is regulated exclusively by the tribes, includes traditional forms of Indian gaming played in connection with tribal ceremonies. Betting on horse racing at a tribe's annual powwow qualifies as traditional gaming. Class II gaming includes lotteries, bingo, and nonbanking card games authorized by state law or not explicitly prohibited by state law. States have no role in the regulation of class II gaming. Class III gaming includes all forms of gaming that are not Class I or Class II. This category includes casino games, slot machines, and pari-mutuel wagering. Class III gaming may be conducted on Indian lands only if such activities are located in a state that permits gaming for any purpose by any person, organization, or entity, and if such activities are conducted in conformance with a tribal-state compact entered into by the Indian tribe and the state. During the first decade of the IGRA, tribal gambling revenues grew more than thirtyfold, from \$212 million in 1988 to \$6.7 billion in 1997. "As was the IGRA's intention, gambling revenues have proven to be a very important source of funding for many tribal-governments, providing much-needed improvements to the health, education, and welfare of Native Americans on reservations across the United States."

With the development of the Internet gambling industry, companies that run Internet gambling sites will inevitably form alliances with the tribes. These companies will attempt to capitalize on the loose provisions of the IGRA. For example, alliances could result in Internet lotteries or Internet bingo games in which companies claim sovereignty under the provisions of the IGRA. Attempts by Internet gambling companies to circumvent gambling regulations by working with tribes would negatively affect the economy. Tribes that lack technological sophistication could be victimized by these companies. The result could be a regression of the improvements that tribes experienced after the enactment of the IGRA. (Comment, Bib. F.3.)

It has been well established from research done in the area that there is a direct link between tribal gambling laws and Internet gambling. It appears that, by working with and through the Indian tribes, Internet gambling operations have developed a way to legally run Internet gambling operations.

## **2. Constitutional limits**

Several Constitutional limits arise when Congress establishes laws that can directly conflict with laws established by the state. The limits come into conflict with what the states are trying to do (i.e. what they are trying to regulate or deregulate) and act as a barrier to laws the states are trying to establish. Several of these Congressional limits include jurisdictional limits (where the state and government can enforce their laws) and the Dormant Commerce Clause (which cover how and when the state can regulate interstate commerce activities).

### **a. Jurisdictional limitations**

The United States is forced, by Constitutional limits, to maintain jurisdictional boundaries and respect those boundaries within and without of our nation. As quoted in a report regarding Internet gambling:

The enforcement of extraterritorial jurisdiction provides the single largest obstacle in the regulation of Internet gambling. The process of obtaining jurisdiction is difficult when a prosecutor is facing acts that are performed in another state. This process becomes radically more complex when the actions that make up the cause of action are committed in a different country. Likewise, jurisdictional determination is not unique to actions committed online.

(International Jurisdiction, Bib. C.4.)

The federal government itself has admitted the difficult problems that can arise when dealing with enforcement of United States laws upon International entities. It can

also be just as hard to implement state laws upon other states within our own country. Laws are developed to protect our citizens from being prosecuted under different laws that they may be violating but are unaware of. Because of the jurisdictional problems, the state may have hurdles to bypass that may limit its ability to enact, regulate, and enforce new laws regarding foreign jurisdictions.

### **b. Dormant Commerce Clause**

The Commerce Clause (Article I, Section 8, Clause 3) grants give Congress the power to regulate interstate commerce. While states share certain powers with the federal government (e.g. the power to tax their own citizens), the Supreme Court has held that the power to regulate interstate commerce is an exclusive one. When the citizens of the United States ratified the Constitution, and within it the delegation of such regulation to the federal government, there arose a negative inference that States surrendered their power to regulate interstate commerce. Even where Congress chooses not to exercise such power, States cannot regulate (even when Congress sleeps, that dormant power is exclusive). (Dormant Commerce Clause, Bib. B.4.)

However, the Supreme Court recognizes that States may exercise police powers to safeguard their citizens. At times, laws passed under such authority affect interstate commerce. The Supreme Court created the *Pike* test (*Pike v. Bruce Church*) to see whether such a law can survive: so long as state laws do not regulate commerce qua commerce, discriminate against interstate commerce, or overly burden commerce, the courts will refuse to strike them down. Note that where a law has an extraterritorial effect, courts will often presume its purpose was one of economic protectionism and outside a state's police powers. But where a state law does not violate the exclusive

nature of the Commerce Clause (always present, i.e. dormant), and is not preempted by federal law, the state law will survive a constitutional challenge. (International Jurisdiction, Bib. C.4.) Note that so long as the Constitution does not expressly prohibit the action, Congress may delegate power back to the States. But where there is not such express authorization, States may not regulate interstate commerce, even in a vacuum of Congressional action. (International Jurisdiction, Bib. C.4.)

Many could argue that Internet gambling is a form of interstate commerce. Transactions are conducted via the Internet that provide one service to the purchaser of that service. The state, when creating new laws to regulate Internet gambling must be aware that, based upon this clause, the federal government may be able to strike down the newly created laws if it finds that the laws overly burden commerce. Drafters of new regulatory laws must be careful that the laws do not violate the *Pike* test. According to the law of commerce, the regulatory laws will be able to survive a constitutional challenge if they do not openly restrict the free trade of commerce between states.

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**APPENDICES:**