A FEDERAL LAW RESTRICTING INTERNET GAMBLING COULD LEAD TO UNINTENDED AND DEVASTATING CONSEQUENCES FOR STATE LOTTERIES

By Mark Hichar
Hinckley Allen and Snyder, LLP [1]
www.hinckleyallen.com

HINCKLEY ALLEN

When Congress has acted to regulate gambling in the past, there often have been unintended consequences. Thus, for example, when Congress passed the Indian Gaming Regulatory Act (the "IGRA"),[2] it "meant to spur economic opportunity and growth on poverty-stricken and remote Indian reservations … The aim of IGRA was Indian empowerment, … [and] many members believed [their 1988 congressional vote] was authorizing bingo parlors on remote tribal lands."[3] However, "[m]any of those who were meant to benefit from IGRA have not, … [and] today, [the law] might as well be renamed the "Law of Unintended Consequences."[4] Similarly, Congress likely did not anticipate that the Unlawful Internet Gambling Enforcement Act (the "UIGEA")[5] would result in fantasy sports league operators using it as a blueprint for daily sports-based games.[6] Finally, when Congress passed the Wire Act in 1961,[7] the members likely did not expect that four-decades later it would be used to prohibit non-sports-related gambling involving wire transmissions, as it was until the Department of Justice ("DoJ") issued its 2011 opinion that limited the Wire Act to sports-related gambling.[8] As stated by the DoJ in that opinion: "The Wire Act's legislative history reveals that Congress's overriding goal in the Act was to stop the use of wire communications for sports gambling in particular."[9] "Congress's decision to expressly regulate lottery-style games in addition to sports-related gambling in [the Interstate Transportation of Wagering Paraphernalia Act[10]], but not in the contemporaneous Wire Act, further suggests that Congress did not intend to reach non-sports wagering in the Wire Act."[11]

In this publication and elsewhere, much has been written about the possible effects, intended and unintended, of the identical "Wire Act fix" bills introduced on March 26, 2014 by Senator Lindsey Graham (R-SC) and Representative Jason Chaffetz (R-UT).[12] While those bills (collectively, the "Bill") purport to "restore" the Wire Act to the meaning given it prior to the DoJ Opinion, they in fact would result in the prohibition of many lottery activities that today are important to state lotteries' revenue generating efforts.

If the Bill became law, the Wire Act would prohibit a gambling business from using any network involving a wire or like connection, including specifically the "internet,"[13] to transmit in "interstate or foreign commerce":

1) Mark Hichar is a Partner with the law firm Hinckley Allen and Snyder, LLP and the Chair of the firm's Gaming Law Practice Group. Mark is a frequent writer and speaker on developments in Gaming Law and related regulatory actions, and has authored several articles on developments in the laws relating to online gaming. See http://www.hinckleyallen.com/mark-hichar/

2) 25 U.S.C. 2701, et seq.

3) "Unintended Consequences," National Review Online, September 29, 2004, at http://www.nationalreview.com/articles/212361/unintended-consequences/gary-bauer, last accessed August 11, 2014.

4) Id.

5) 31 U.S.C. 5361, et seq.

6) See, for example, FanDuel's explanation of the lawfulness of its games, at: https://www.fanduel.com/legal, last accessed August 8, 2014.

7) 18 U.S.C. §§ 1081 and 1084.

8) Memorandum Opinion for the Assistant Attorney General, Criminal Division, "Whether Proposals by Illinois and New York to Use the Internet and Out-of-State Transaction Processers to Sell Lottery Tickets to In-State Adults Violate the Wire Act," September 20, 2011 (issued December 23, 2011) (the "DoJ Opinion").

9) Id., at page 8.

10) 18 U.S.C. § 1953.

11) DoJ Opinion, at page 11.

12) S. 2159 and H.R. 4301, respectively.

13) "Internet" is not defined in the Bill, nor is it defined in the Wire Act (which was enacted decades before the internet existed). Thus, courts looking for its meaning would likely refer to the Unlawful Internet Gaming Enforcement Act (the "UIGEA") (31 U.S.C. § 5361 et seq.). There, "internet" is defined as the "international computer network of interoperable packet switched data networks." (31 U.S.C. § 5362(5)).

(A) any bet or wager, or

(B) information assisting in the placing of any bet or wager,[14] or

(C) a communication entitling the recipient to receive money or credit as a result of any bet or wager.

However, the Bill contains four exemptions, which would:

(1) preserve the status quo as to internet betting on horse races;[15]

(2) preserve the status quo as to internet betting on charitable games;[16]

(3) not apply to pay-for-play online fantasy sports tournaments conducted in accordance with the UIGEA; and

(4) not change or limit "the ability of a State licensed lottery retailer to make in-person, computer-generated retail lottery sales under applicable Federal and State laws in effect on the date of the enactment of [the Bill]." Thus, "in-person" lottery sales by licensed lottery retailers would remain lawful to the extent they were lawful before the Bill became law.

Of course, among the Bill's intended consequences is a ban on sales of lottery games via PCs and/or mobile devices. However, if the Bill became law, there would be other, seemingly unintended consequences to state lotteries. For example, due to the wording of the Bill's fourth exemption (the "Lottery Exemption"), the amended Wire Act would render unlawful the operation of a state lottery (including traditional online games) by any current non-lottery state that had not enacted lottery legislation by the date the Bill became law.

In addition, due to the ambiguity of the "in person" sales requirement in the Lottery Exemption, the exemption likely would not cover and thus it would be unlawful for a state lottery to (1) operate video lottery games where the video lottery terminals exchanged wagering information (even if not actual wagers) with a central system via the "internet" (i.e., a network of interoperable packet switched data networks), or (2) to sell lottery games via player-activated terminals (because such terminals exchange wagering information with a central system via the internet). This would be true even if the wager-related transmissions were between points in the same state, because the Bill clarifies that the phrase "uses a wire communication facility for the transmission in interstate or foreign commerce," as used in the Wire Act, "includes any transmission over the Internet carried interstate or in foreign commerce, incidentally or otherwise." (emphasis added) Thus, if the intermediate routing of the wager-related transmissions crossed state lines (or was considered to cross state lines), it would violate the Wire Act, when the Lottery Exemption did not apply.[17]

Advocates of the Bill have claimed that state lotteries' concerns about video lottery gaming and player-activated terminals are unwarranted, and that the Lottery Exemption would exempt from prohibition such lottery activities.[18] However, the Lottery Exemption does not appear to "carve-out" such lottery gaming, and thus state lotteries' concerns are indeed valid.

Specifically, courts and regulators have often distinguished between "in-person" sales and sales via vending machines. For example, in 1993 a California court was called upon to determine whether a California state law governing the sale of cigarettes preempted a local ordinance adopted by the City of Rancho Mirage.[19] Describing the state law, the court stated that it "identifies the person liable in the event the proscribed sale is accomplished through a vending machine rather than in person."[20] The Court thus distinguished between sales via a vending machine and "in person" sales (the latter being over-the-counter sales by a sales clerk), making clear that they were different methods of sale. The Washington Supreme Court made a similar distinction, noting in a 2008 opinion, that in an earlier case, it "struck down an ordinance taxing vending machines but not-in person sales."[21] Finally, Providence, Rhode Island is among the cities that distinguish between "in-person" sales of tobacco products and sales of such products via a "vending machine."[22]

Thus, because courts and regulators in other contexts have distinguished between "in-person" sales and sales via a vending machine, concerns regarding the Bill's application to video lottery and player-activated lottery sales terminals are valid. Looking to the above cases and regulations as guidance, a court could interpret the Lottery Exemption in the Bill as not applying to—and thus not preserving—the ability of state lotteries to (1) conduct video lottery gaming where the video lottery terminals exchange wagering information with a central system over a wide area network, or (2) sell lottery tickets via vending machines or by any method other than over-the-counter sales involving personal interaction between a sales clerk and a purchaser.

The above illustrates but two unintended consequences of the Bill—the elimination of player-operated lottery ticket vending machines and the prohibition of certain video lottery games. Others would no doubt become evident if the Bill were to become law. (One consequence of the Bill that seems entirely intentional, incredibly, would be its elimination of certain rights Indian tribes had prior to the DoJ's 2011. Nothing in the Bill addresses Indian gaming, and the concerns of Indian tribes have simply been ignored.)[23]

In summary, as has been the case when Congress regulated gaming in the past, if the Bill became law, there would be unintended consequences, and those affecting state lotteries could be devastating in effect. For this reason, among others, the regulation of internet gaming should be left to the individual states—which historically have been allowed to regulate gaming occurring within their borders. States have historically performed this regulatory responsibility prudently and wisely, keeping in mind the sensibilities of their citizenry. ◆

14) However, there would be an exception for the transmission of information assisting in sports betting (but not actual bets) transmitted between states in which betting on such sports events was lawful.

15) It is generally accepted that internet betting on horse races is lawful under a 2000 amendment to the Interstate Horseracing Act (15 U.S.C. § 3001 et seq.).

16) Thus, to the extent internet betting on such games were lawful under state laws in effect on the date the Bill became law, it would remain lawful.

17) Note, in this regard, that the U.S. courts of appeal in the 1st, 3rd and 5th federal circuits have held that transmissions via the internet are considered to be in interstate commerce, regardless of the actual routing. "[B]ecause of the very interstate nature of the Internet, once a user submits a connection request to a website server…data has traveled in interstate commerce." U.S. v. MacEwan, 445 F.3d 237, 244 (3rd Cir. 2006); "Transmission…by means of the Internet is tantamount to moving [data] across state lines." U.S. v. Carroll, 105 F.3d 740, 742 (1st Cir. 1997), followed by U.S. v. Runyan, 290 F.3d 223 (5th Cir. 2002) and by U.S. v. Yong Wang, 2013 U.S. Dist. LEXIS 16153 (S.D.N.Y. 2013).

18) See, for example, "Lotteries, Retailers Clash Over 'Unintended Consequences' of Wire Act Fix," Gambling Compliance, May 14, 2014, by Tony Batt, in which NACS attorney Douglas Kantor is quoted referring to such claims as "misleading" and "fantasy land."

19) Bravo Vending v. City of Rancho Mirage, 20 Cal. Rptr. 2d 164 (Cal. Ct. App., 4th App. Dist. 1993).

20) Id., at 174 (emphasis added).

21) Ventenbergs v. City of Seattle, 178 P.3d 960, 975 (Wa. 2008), referring to City of Seattle v. Dencker, 108 P. 1086 (1910).22 Providence, Rhode Island Code of Ordinances, Article XV, sec. 14-303 (2013).

23) This is in contrast to the UIGEA and other federal bills that sought to regulate internet gaming. For example, although deeply flawed, the UIGEA at least expressly provides that the term "unlawful Internet gambling" does not include sending or receiving bets or wagers within the Indian lands of a single Indian tribe or between the Indian lands of two or more Indian tribes (to the extent that intertribal gaming is authorized by the Indian Gaming Regulatory Act (25 U.S.C. § 2701 et seq.) and meets certain other conditions in the UIGEA. 31 U.S.C. § 5362(10)(C). Similarly, the "Internet Gambling Prohibition, Poker Consumer Protection, and Strengthening UIGEA Act of 2010, drafted by Senator Harry Reid's office in late 2010 but never introduced (the "Reid Bill"), expressly "carved out" such wagering within tribal lands. Reid Bill discussion draft, Title I, Section 102(2)(B)(iv) on page 12.