

Clients & Friends Memo

Time to Roll the Dice on Online Gaming?

January 12, 2012

On December 23, 2011, the U.S. Department of Justice Office of Legal Counsel (“OLC”) issued a memorandum opinion dated September 20, 2011, eliminating one of the federal barriers to legalizing internet gambling and opening the door for the possibility of a regulatory regime shift.¹ In the [OLC Opinion](#), the Department of Justice addressed an apparent conflict between the Wire Act and UIGEA and concluded that “interstate transmissions of wire communications that do not relate to a sporting event or contest” fall outside the reach of the Wire Act. Finding that the Federal Wire Act does not prohibit the use of out-of-state transaction processors to sell in-state lottery tickets over the internet or the transmission of lottery data across state lines, the OLC Opinion reverses the long-held position that the Wire Act applied to all interstate gambling, whether sports-related or not. Although it may take some time to determine the ultimate effect of the OLC Opinion, now that the Justice Department has clarified its view that the Wire Act does not broadly prohibit online wagering (unless it relates to sporting events or contests), the advance of internet gaming appears inevitable.

The Wire Act & The UIGEA

The Federal Wire Act, 18 U.S.C. § 1084 (2006), provides, in relevant part that:

Whoever being engaged in the business of betting or wagering knowingly uses a wire communication facility for the transmission in interstate or foreign commerce of bets or wagers or information assisting in the placing of bets or wagers *on any sporting event or contest*, or for the transmission of a wire communication which entitles the recipient to receive money or credit as a result of bets or wagers, or for information assisting in the placing of bets or wagers, shall be fined under this title or imprisoned not more than two years, or both.

¹ Whether Proposals by Illinois and New York to Use the Internet and Out-of-State Transaction Processors to Sell Lottery Tickets to In-State Adults Violate the Wire Act (2011), <http://www.justice.gov/olc/2011/state-lotteries-opinion.pdf>.

18 U.S.C. 1084(a) (emphasis added). Section 1084(a) is split into two clauses: the first clause prohibits using a wire communication for the transmission in interstate or foreign commerce of (i) “bets or wagers” or (ii) “information assisting in the placing of bets or wagers.” The second clause prohibits the use of a wire communication as a means of transferring money or credit (i) “as a result of bets or wagers,” or (ii) “for information assisting in the placing of bets or wagers.” The OLC Opinion makes clear the Justice Department’s view that both clauses should be limited in application to sports-related wagers.

In 2006, Congress enacted the Unlawful Internet Gambling Enforcement Act (“UIGEA”), 31 U.S.C. §§ 5361-5367 (2006), which prohibits internet gambling in a jurisdiction where applicable federal or state law makes such bets illegal. 31 U.S.C. §§ 5363, 5362(10)(A). Importantly, the UIGEA provides an exception for bets “initiated and received or otherwise made exclusively within a single State,” and expressly provides that the “intermediate routing of electronic data shall not determine the location or locations in which a bet or wager is initiated, received, or otherwise made.” 31 U.S.C. § 5362(10)(B) and (E).

The Opinion

The Criminal Division of the Justice Department has historically taken the position that the Wire Act is not limited to sports-related wagering and can be applied to other forms of gambling involving interstate information or funds transfer. However, the Criminal Division’s interpretation of the Wire Act is inconsistent with the language of the UIGEA, which specifically permits out-of-state routing of data associated with lawful in-state transactions. Given the tension between the Criminal Division’s interpretation of the Wire Act and the UIGEA, the Criminal Division requested an opinion from the OLC to clarify whether the Wire Act and the UIGEA prohibited the proposed expansion of the New York and Illinois state lotteries to allow for the in-state purchase of lottery tickets over the internet. Under these proposals, the purchaser and seller of the ticket would both be located in the same state but the transaction processor would be located out-of-state and certain transaction data would be routed across state lines.

Relying on statutory interpretation principles and legislative history, the OLC concluded that the Wire Act only applies to a “sporting event or contest” and therefore, did not govern the New York and Illinois lottery proposals. First, the OLC determined that the Criminal Department’s position that the phrase “any sporting event or contest” modifies only the second part of the first clause of section 1084(a) was illogical – why would Congress forbid actual bets or wagers for all types of gambling while only prohibiting transferring information assisting bets or wagers if the bets or wagers were sports-related. Rather, the OLC concluded that the most logical reading of the first clause of section 1084(a) is that the phrase “any sporting event or contest” modifies both instances of “bets and wagers” so that “both provisions are limited to bets or wagers on or wagering communications related to sporting events or contests.” OLC Opinion at 5. The OLC found that it

was reasonable to assume that Congress intended to prohibit the transmission of information about wagers in a manner that covers a similar scope to the actual forbidden wagers. Second, relying on the legislative history of section 1084(a), the OLC concluded that as originally proposed, section 1084(a) clearly limited the scope of transmissions of wagers and information related to wagers only to sports-related gambling. Because the legislative history did not indicate Congress's intention to broaden the scope of section 1084(a), the OLC found that the entire first clause of section 1084(a) was limited to sports-related gambling.

The OLC next determined that the second clause of section 1084(a), which prohibits the transmission of winnings, is similarly limited. The OLC concluded that reading all of section 1084(a), including the second clause, as being limited to sports-related gambling made functional sense because all of the subsections' prohibitions would serve the same end - to forbid wagering, information transfer and winnings transmissions on sports-related gambling. Additionally, the OLC found that the legislative history of section 1084(a), which reflected Congress's overriding goal to stop the use of wire communications for sports gambling, supported its reading of the subsection. Finally, the OLC found it instructive that on the same day that Congress passed the Wire Act, it also passed another statute that expressly regulated lottery-style games in addition to sports-related gambling. Accordingly, the OLC reasoned that if Congress intended to incorporate non-sports related wagering into the Wire Act, it would have done so explicitly.

As a result of this analysis, the OLC concluded that the New York and Illinois lottery proposals were not prohibited under the Wire Act. Having so determined, the OLC concluded that it did not need to consider how to reconcile the Wire Act with UIGEA because the two statutes were not in conflict under the facts presented. The facts in question involved in-state sales of lottery tickets, with data transmission crossing state lines for processing. Notably, the OLC Opinion did not address interstate wagering on non-sports related activities.

Ramifications

It is difficult to predict what the regulatory framework of internet gambling will look like in the future. Although the OLC Opinion was issued in response to a question regarding in-state lottery sales, the broad language in the OLC Opinion indicates that the traditional federal prohibition of internet gaming based on the Wire Act may no longer be operative. The elimination of the Wire Act as a barrier to internet gambling, leaves only individual state anti-gambling laws and the UIGEA to provide statutory prohibitions to internet gaming. This suggests that bets placed online between two states, where such wagering is legal, would not be prohibited under Federal Regulations. It remains to be seen whether the OLC Opinion triggers a push in Washington to enact a new regulatory regime as federal regulators accustomed to having jurisdiction via the Wire Act may not be willing to cede control of the sector to a patchwork of state laws and regulations.

That said, the day-to-day regulation of gaming companies is currently a state function. Accordingly, states may attempt to enact regulations that encompass online as well as traditional land-based gaming. Currently, Nevada is the only state to pass legislation that provides the regulatory framework for legal internet poker. Since the release of the OLC Opinion, some New Jersey legislators have floated similar proposals. However, industry observers do not believe that Nevada or any other small state can provide enough in-state online players to successfully launch an online poker site. As a result, if the federal government does not issue a consistent regulatory scheme governing all states, it does not appear likely that a large amount of online poker will take place in the U.S. until enough states enact online gaming regulations.

Additionally, although the release of the OLC Opinion touched off a rally in the shares of some traditional gaming companies, it is unclear whether these companies will be willing to commit to online poker until the regulatory atmosphere is clarified. Given the FBI's previous actions – including arrests and domain name seizures of internet poker sites in April, 2011 – it is unlikely that established gaming companies will jeopardize their existing gaming licenses by acting prematurely. It is more likely that these companies will refrain from entering this market until the new regulatory framework takes shape. Once more regulatory clarity is achieved, it may still take some time for established gaming companies to migrate online as these companies tend not to have the necessary experience to operate websites that accept wagers. Established gaming companies could speed up the process by partnering with existing online gaming companies to license software and other technology. Several joint ventures of this type have already been formed.

Ultimately, given the recent change in the Justice Department's view of the Wire Act, the questions now revolve around the details of *when* and *how* online gaming will evolve as opposed to whether legal online gaming will ever become a reality in the U.S.

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