

Tainted asset rules decrease US state i-gaming success

A number of US states are moving towards regulating online gaming and have proposed i-gaming laws in the hope that regulation will soon follow. However the number of states to include a 'tainted assets' provision, which excludes any participants of 'Black Friday' from being part of the regulated market, could potentially damage the as yet untapped US online gambling market. Sarah Coffey, an Associate at Ibrah Law, a Washington, DC-based law firm specialised in gaming law, discusses the current situation and examines the potential harm a 'tainted assets' provision could cause.

After the shutdown of major i-gaming websites in the United States on 'Black Friday,' 15 April 2011, American states identified online poker as an untapped market that could draw in substantial profits to boost flagging state economies. There has been a resulting effort to push through legislation to implement real-money intrastate online poker games. In doing so, however, states have been lobbied to exclude i-gaming providers that operated in the United States after 2006 - the year the Unlawful Internet Gambling Enforcement Act (UIGEA) was passed - under the theory that such operators would be using 'tainted assets' derived from 'illegal' poker operations. This prohibition is shortsighted and self-serving to the interested parties lobbying for it, and would only serve to impede the success and profitability of states' i-gaming programs. States should drop such provisions before passing i-gaming bills into law.

A number of states including California, Florida, and New Jersey

have considered including a tainted assets provision in proposed i-gaming laws. Of all the states considering this proposal, however, New Jersey is the state where it would have the most significant ramifications, given the state's long history of gambling regulation.

New Jersey

New Jersey's proposed online gaming bill has undergone various amendments in advance of a final vote, which is expected in fall 2012. So as not to threaten the business of the state's brick-and-mortar casinos in the gambling hub of Atlantic City, only those casinos with a physical presence can operate i-gaming operations throughout New Jersey. Since online gaming inherently requires a different set of technology and expertise than land-based casinos, it is expected that casinos will team with experienced i-gaming operators to offer secure, complaint, and glitch-free i-gaming platforms.

However, a proposed addition to Section 37 of New Jersey's bill would place significant restrictions on the i-gaming providers that would be permitted to team with casinos to offer these services. The current Assembly version of the bill prohibits a corporation or any person seeking to provide goods or services to a casino licensee from doing business with a casino in connection with internet gaming if they 'at any time, either directly or through another corporation or person it owned in whole or in significant part, or controlled' knowingly accepted or made available bets, wagers, or stakes using the internet from persons located in the United States after 31 December 2006 or 'knowingly facilitated or otherwise provided services' with respect to the same.

The tainted-assets clause of the proposed law states that

corporations and persons also shall not be permitted to conduct business with a casino if they 'purchased or acquired, directly or indirectly, in whole or in significant part' the assets of a company that offered such services post-2006. This ban shuts out some of the biggest, most experienced names in online gaming.

The New Jersey bill's cutoff date of 2006 roughly corresponds to the implementation date of UIGEA, a federal law which regulates gambling payments made over the internet but which left to the states' discretion what constituted a prohibited game of chance. (The law was actually passed in October 2006). The New Jersey bill's broad language prohibiting the participation of anyone who provided 'goods or services' post-2006 applies not only to those who had 'control' over those i-gaming companies, but also to a broad range of vendors including those offering software, advertising, or computer programming to the i-gaming companies.

It is thought that some of the major Atlantic City casinos have already negotiated to team with i-gaming providers that have not operated in the U.S. after 2006. For instance, Ceasars has allegedly negotiated with 888 Holdings, and the Borgata hopes to team with Bwin Party. While there is no word that official deals have been reached, casinos and providers have lobbied for the inclusion of the tainted assets provision so as to eliminate competition from rival providers. Lobbyists have convinced some New Jersey legislators that these restrictions will protect the interests of the state's existing casinos. Since online gaming is a hotly contested issue, legislators may also believe that the bill is more likely to pass if it distances itself from companies

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such as those shut down during the Black Friday seizures and whose officers and employees are currently subject to indictment and class action lawsuits. It is against New Jersey's interests to include these unnecessary restrictions in their online gaming bill. Any state that wants to achieve the maximum benefits for its own interests and economy should not include such restrictive tainted assets provisions.

Most obviously, casinos and online gaming companies choosing where to locate will want to go to the state with fewest restrictions on how they operate their business. For instance, Nevada - perhaps the state most associated with gambling and most familiar with its regulation - recently passed an online gaming bill that did not contain a tainted assets provision. Given the choice of setting up shop in Nevada or New Jersey with their respective i-gaming laws in place, gaming companies will likely choose Nevada because it has the fewest obstacles to operational approval and success.

Nevada

While Nevada's i-gaming law, like many state gambling statutes, requires a suitability determination for licensees (essentially reviewing applicants for issues concerning honesty, integrity, and good moral character, including a criminal history check), such determinations are much more fluid than the complex, fact-intensive inquiry required by the 'tainted assets' provision. A New Jersey casino would have to scrutinize the history of every employee, vendor, and contractor who will be associated with the online gaming venture to determine their connection to prior providers, because each one of those people could put the online gaming license in jeopardy.

States are heading in the right direction by enacting legislation to implement legal, state-regulated online gaming. However the overly cautious approach that some states are taking in regard to prior providers presents unnecessary self-imposed obstacles to the ultimate success of this industry.

By excluding companies and individuals connected with post-2006 online poker in the U.S., New Jersey is also eliminating some of the most experienced names in the business. Companies such as Full Tilt, Poker Stars, and Absolute Poker have years of experience administering all aspects of online gaming ventures and are in the best position to hit the ground running in New Jersey. They know the ins and outs of the security, software, and money transfer platforms necessary to offer i-gaming on a large scale. Less experienced operators are likely to be plagued with glitches that could compromise the viability of a long-term program, and are likely to offer an inferior product that will not draw in users. Consumers want access to the best technology available, and there should be free and open competition to offer that product. Even if New Jersey were to pass the bill with these restrictions, they could ultimately be struck as unconstitutional on a number of grounds-including violations of the Due Process Clause and Takings Clause, to name a few-subjecting the state to protracted, unnecessary, and avoidable litigation.

Since operators would be excluded for operating after the arbitrary date of 31 December 2006 - rather the date UIGEA was signed into law on 13 October 2006 - the provision could violate the Due Process Clause of the U.S. Constitution because providers were arbitrarily deprived of a significant property interest without prior notice or a meaningful opportunity to be heard. The New Jersey cutoff date is especially notable because it serves to exclude providers who operated into 2007 while including providers that ceased operating in late 2006, even though both continued operating after UIGEA

was signed into law.

A legislative prohibition on operating in a lawful market could also be an unconstitutional taking under the Fifth Amendment of the U.S. Constitution, which is applicable to the states through the Fourteenth Amendment. That clause states that private property shall not 'be taken for a public use without just compensation.' Since the New Jersey law prohibits prior providers from selling their most valuable assets to the New Jersey casinos, it impairs the value of that property by rendering it valueless in that state, and less valuable overall.

States are heading in the right direction by enacting legislation to implement legal, state-regulated online gaming. However the overly cautious approach that some states are taking in regard to prior providers presents unnecessary self-imposed obstacles to the ultimate success of this industry. States such as New Jersey should drop the tainted assets language before voting to enact i-gaming. The best way for states to succeed in online gaming is to offer competitive markets where all are able to compete to offer the best services to consumers. Without that, these programs are only heading for trouble.

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