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Betting on the U.S. Market

A Discussion of the Legality of Sports Gaming Businesses¹

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ABSTRACT: Over time, the US sports gaming industry has progressed dramatically beyond what the US anti-gaming law drafters envisioned. The result is a system of mostly antiquated laws controlling modern industry causing confusion across the board. This discussion, therefore, intends to shed light on the US sports gaming legal framework, including analysis of the preeminent US laws that regulate the sports gaming industry and a brief review of various sports gaming businesses that fall within the US legal rubric.

Keywords: sports betting, gaming, Internet gaming

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Introduction

The US market for sports gaming activities is established and growing. In 2009 alone, the legal horserace parimutuel pools took in gross US bets² of US \$12.3 billion (Angst, 2010).³ The state of Nevada has race betting as well, but also is the only state with virtually unrestricted legalized sports betting similar to that commonly found outside the United States. In 2009 and 2010, Nevada gross legal sports bets amounted to \$2.6 billion and \$2.8 billion, respectively, and gross legal race bets amounted to \$400 million and \$381 million, respectively (State

of Nevada, 2009, 2010). Yet, as large as these industry numbers are, they do not include the overwhelming amount of illegal betting conducted in the United States each year. While it is difficult to accurately quantify the size of the illegal betting market since, at the very least, its illegality tends toward nondisclosure, a recent investigative news report estimated the three sports that garner the majority of illegal US bets are football (US version), basketball, and baseball, with approximately \$255-\$300 billion bet annually ("Top Sports for Illegal Wagers," 2009). Although the accuracy of this estimate is indeterminable, it is fair to say that the

illegal gambling market is indeed quite significant. These figures also do not include gaming revenues from sports-related games not traditionally considered gambling, such as fantasy sports, which alone in 2009 accounted for additional annual revenues of \$1.5 billion in the United States (Ankeny, 2009; Dahle, 2008; Spaeder, 2009).

It is understandable that given the enormity of these figures and the success of interactive gaming companies with their recent billion-dollar valuations, companies want to participate in the US sports gaming market (Levy & Satariano, 2009). However, it may not be readily apparent which activities are permissible under US law or how those activities must be structured to comply with US law.

At times, the legality of sports gaming in the United States can appear to be in a constant state of flux. Courts and companies continually grapple with interpreting antiquated anti-gaming laws for a modern gaming industry. Special interests, such as political conservatives, regularly seek to enact additional anti-gaming laws and diminish gaming opportunities while others, such as gaming operators, simultaneously seek to test the limits of, modify, and expand the same. Moreover, the myriad of US laws, court decisions, US Department of Justice (DOJ) legal stances (and eventual prosecutions), and sports gaming operations create divergent views and arguments as to which forms of sports gaming are legal in the United States.

This state of confusion and concern regarding the legality of sports gaming activities has led some US- and EU-based businesses to operate in the United States only later to find they are defending prosecution or negotiating settlements with the Department of Justice (“BetOnSports Fined \$28 Million,” 2009; Richtel, 2004; Ryan, 2007; *United States v. \$6,976,934.56*, 2006; *United States v. Betonsports PLC*, 2006; *United States v. John David Lefebvre*, 2007; *United States v. Stephen Eric Lawrence*, 2007). Such confusion has been amplified by the recent World Trade Organization (WTO) dispute

challenging the US position on horserace betting, but as we illustrate later, each side of this dispute was, in fact or in effect, arguing in error. Consequently, the ultimate rulings in the WTO dispute arose from an incorrect understanding of the US anti-gaming laws.

The purpose of this review, therefore, is to explain the framework of US sports gaming laws and set forth forms of sports gaming activities that are permitted in the United States.

US Legal System

Before embarking on an analysis of US sports gaming laws, a brief review of the US legal system is beneficial. The United States has a two-tier structured government divided between the federal and state governments (Chemerinsky, 2002). Federal law is enacted by the US Congress—the legislative arm of the federal government—and is supreme to law enacted by each state. The federal government, however, can only pass laws if it has clear authority to do so. Otherwise, governance is left to the states (Chemerinsky, 2002).

Correspondingly, there are two court systems split between the federal and state jurisdictions. The federal and state court systems are divided regionally and operate on a vertical hierarchy within each region. At the federal level, the highest court is the US Supreme Court, followed by the 13 regional US Circuit Courts of Appeal, and then the regional US District Courts that fall within one of the 13 federal appellate circuits. A similar system exists at the state level, wherein most commonly each state has a supreme court, followed by a court of appeals, and then district courts (Burnham, 2002).

Not all court decisions are binding on all courts. The US Supreme Court decisions are binding on all federal and state courts. However, within each regional federal and state court system, the decisions of higher courts are binding on the lower courts, but the decisions of courts outside each respective region are only persuasive, not binding (Chemerinsky, 2002). The federal courts only hear certain cases, most

commonly involving questions of federal law but also may include state law. In interpreting federal law, the federal courts follow precedent within their respective region up to the US Supreme Court and may look to other federal regions for interpretations of the law that are persuasive but do not require mandatory compliance (Chemmerinsky, 2002). The state courts hear almost any type of case other than cases that are heard exclusively by the federal courts. Similarly, in interpreting state law, the state courts follow precedent within their respective region up to the US Supreme Court and may look to other state regions for persuasive interpretations (Burnham, 2002). Additionally, the state courts may interpret federal law if applicable to the case before the state court, which is subject to review by the federal courts.

Federal Gaming Regulation

With some exceptions, the federal government has not traditionally played a major role in regulating the gaming industry (Gottfried, 2004). Instead, gaming regulation and enforcement has been viewed as most appropriate for states—that is, to allow each state to decide which gaming activities are legal.⁴ One of the first instances of federal regulation can be traced back to 1890, when Congress passed a law prohibiting the sale of lottery tickets through the mail. Congress passed the law in response to the Louisiana lottery, a notorious lottery that was run by a New York syndicate to promote bribery. Following the introduction of the federal law, the state legislature shut down the lottery two years later (Thompson, 1994). Then, in 1951 Congress passed the Gambling Devices Act of 1951. This Act, as amended by the Gambling Devices Act of 1962, supplements state law by prohibiting the interstate transportation of gambling devices into jurisdictions where their manufacture or possession is not specifically legal, and imposing registration and recordkeeping requirements on those who manufacture and distribute the devices for public use (Cabot, 1998). Similar to the 1890 legislation, the Gambling Devices Act of 1951 was introduced

to combat organized crime associated with the proliferation of gambling in the United States. Specifically, the Gambling Devices Act of 1951 was the result of a report published by the US Senate Special Committee on Investigative Organized Crime in Interstate Commerce that concluded “organized criminal gangs operating in interstate commerce are firmly entrenched in our large cities in the operation of many different gambling enterprises . . . as well as other rackets. . . .” (Kefauver, 1951, p. 1). Moreover, beginning in the 1960s, the federal government determined the states needed assistance in enforcing their laws against unlawful gaming activities, particularly organized crime, and proceeded to pass a series of federal anti-gaming laws.

Most of these more recent federal laws merely prohibit the offering of gaming activities in states where such activities are already illegal under state law (Gottfried, 2004). Consequently, federal gaming laws, in general, do not replace state laws; rather, they protect them from circumvention in interstate and foreign⁵ commerce (Shaker, 2007). The DOJ is the chief law enforcement agency of the United States and plays a prominent role in preventing circumvention in interstate and foreign commerce by enforcing US federal gaming laws and prosecuting persons violating those laws.

The Wagering Paraphernalia Act

The Federal Wire Wager Act of 1961 (Wire Act) is the preeminent federal law controlling the sports betting industry; however, several other acts are worth noting. For instance, while certainly less prominent than the Wire Act, the Interstate Transportation of Wagering Paraphernalia Act of 1961 (WPA; 2009) was enacted as part of the same federal legislation as the Wire Act and on the very same day. The WPA criminalizes the interstate and foreign transportation “of any record, paraphernalia, ticket, certificate, bills, slip, token, paper, writing, or other device used, or to be used, adapted, devised or designed for use in” bookmaking, wagering pools with respect to a sporting event, or a

numbers policy, bolita, or similar game (US Code & Cong. News, 1961).

The WPA is intended to accomplish a very specific function: “It erects a substantial barrier to the distribution of certain materials used in the conduct of various forms of illegal gambling” by cutting off supplies used in illegal gaming (*Erlenbaugh v. United States*, 1972, p. 246). When drafting the WPA, Congress employed broad language to “permit law enforcement to keep pace with the latest developments” (*United States v. Mendelsohn*, 1990, p. 1187). As a consequence, many of the WPA’s terms are general, undefined, and unspecific, such as “paraphernalia,” “paper,” “writing,” and “device.” This enables the DOJ and US courts to interpret and apply the WPA’s prohibitions as needed for the circumstances at hand.

For example, in *United States v. Mendelsohn*, the court held that a computer disk containing a software program for recording and analyzing bets on sporting events is wagering paraphernalia (*United States v. Mendelsohn*, 1990). Similarly, in *People v. World Gaming*, a New York State court declared that an Internet gaming website located in Antigua violated the WPA by sending records of illegal gaming activity into the state of New York (*People v. World Gaming*, 1999, p. 852). Moreover, the court further held that the Internet gaming operator violated the WPA by sending computers from the United States to Antigua that would ultimately be used for conducting illegal gaming operations between the United States and Antigua (*People v. World Gaming*, 1999, p. 853). Thus, practically any tangible devices, including software and electronics, intended to be used in illegal gaming activities, regardless of whether they have uses outside those activities, are encompassed in the WPA’s prohibitions.

Due to the breadth of the WPA’s prohibitions, exceptions are included in the WPA to clarify which activities are legal. Without the inclusion of these exceptions, the transportation of any wagering paraphernalia across state lines would be illegal regardless of the legality of gaming or possession of such

paraphernalia in either the state that is sending paraphernalia to or receiving paraphernalia from another state or foreign jurisdiction. Some of the WPA exceptions include (1) wagering materials carried by a common carrier (e.g., the US Postal Service) in the usual course of business; (2) pari-mutuel betting equipment or tickets where legally acquired; (3) pari-mutuel materials used at racetracks or other sporting events where state law allows such betting; (4) betting materials to be used to place bets or wagers on a sporting event into a state whose laws allow such betting; (5) any newspaper or similar publication; (6) equipment, tickets, or materials to be used in a state-run lottery; and (7) equipment, tickets, or materials designed to be used and transported to a foreign country for a legal lottery (Cabot, 1998).

The Federal Wire Wager Act

Whereas the WPA focuses upon tangible items, the Wire Act, in contrast, applies to intangible items. Specifically, the Wire Act prohibits using almost any known interstate or foreign communications medium for transmitting bets, transmitting information assisting in placing bets, or transmitting information entitling a person to credit or money as a result of a bet on any sporting event or contest (Federal Wire Wager Act of 1961, 2009). Subsection 1084(a) sets forth the Wire Act’s prohibitions.

Whoever being engaged in the business of betting or wagering knowingly uses a wire communication facility⁶ 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.

Subsection 1084(b) of the Wire Act also contains a much-cited exception known as the “safe harbor” provision.

Nothing in this section shall be construed to prevent the transmission in interstate or foreign commerce of information . . . assisting in the placing of bets or wagers on a sporting event or contest from a State or foreign country where wagering on that sporting event or contest is legal into a State or foreign country in which such wagering is legal.

The safe harbor only applies to the transmission of “information assisting in the placing of bets,” not to the transmission of (1) bets or (2) wire communications entitling the recipient to money or credit as a result of bets. The exception is further narrowed by its requirement that the betting at issue be legal in both jurisdictions in which the transmission occurs (Federal Wire Wager Act of 1961, 2009).

At first blush, this seems to be clear enough. However, the Wire Act is extremely poorly written, to the point of being incomprehensible in parts. For example, Subsection 1084(a) is a single sentence containing 94 words (Cabot, 2010). In practice, this has led to considerable debate and confusion regarding the breadth of the Wire Act.

Even the first ten words of the Wire Act, which appear to be the clearest, require interpretation by the courts since Congress failed to define what exactly qualifies as being “in the business of betting or wagering” (Federal Wire Wager Act of 1961, 2009). Essentially, the courts have found this requires that a person not only be engaged in the “sale of a product or service for fee” (*United States v. Barborian*, 1981, p. 329), but that the person also be engaged in a “continuing course of conduct” (*United States v. Scavo*, 1979, p. 843). Accordingly, where a gaming operator charges customers for its service, such as charging fees for accepting or brokering bets, this would be the continuing activities that equate to a business operation and will likely constitute being “engaged in the business of betting or wagering,” thus

leaving them open to liability under the statute (Federal Wire Wager Act of 1961, 2009; *United States v. Scavo*, 1979, pp. 841–843). The Wire Act does not, however, go after the casual gambler.⁷

The *United States v. Cohen* case found an Internet sports betting operation was in the business of betting or wagering and established the applicability of the Wire Act to Internet sports betting in foreign commerce (*United States v. Cohen*, 2001). Cohen operated an offshore sports betting company—the World Sports Exchange (WSE)—based in Antigua that accepted bets on a wide range of sports (“Man Jailed in 1st Online Gambling Conviction,” 2000). Patrons would establish and fund accounts with the company in Antigua typically through wire transfers, and the company would only place bets from those Antiguan accounts. However, the company would take telephone calls and Internet communications from US patrons where the patrons would relay information on which bets the company should place using funds from their Antigua accounts. Cohen maintained that the Wire Act should not apply because his business was licensed in Antigua and all bets were taken, recorded, and processed in Antigua. The court, on appeal from his conviction, held that the bets take place both in the state where the bettor resides and where the servers or service provider resides; therefore, the bets took place at least in part in the state of New York. Since the bets took place in the United States, the court held the Wire Act applied, and Cohen’s conviction for violating the Wire Act was upheld.

Of greater debate is whether the Wire Act applies to betting on nonsports gaming. The debate centers on whether the Wire Act is read to apply to any “sporting event” and “sporting contest,” or “sporting event” and “contest,” which in the later case is seen as a prohibition of not only sports betting but also all other types of betting contests (Rodefer, 2004). The DOJ’s official position is that “contest” is distinct from “sporting event” and that Internet casino games, among others, are “contests”; thus, the DOJ concludes that using

interstate and/or foreign communications media for betting on Internet casino games is prohibited under the Wire Act (Hearing on Establishing Consistent Enforcement Policies in the Context of Online Wagers, 2007).

Contrary to the DOJ's position, the Wire Act's legislative history and wording permits a strong argument that it pertains only to sports betting, as the Wire Act explicitly enumerates "sporting event or contest," with the word "sporting" predicating both the word "event" and "contest" (Federal Wire Wager Act of 1961, 2009). This is supported by the US Court of Appeals for the Fifth Circuit (a federal court) ruling that the Wire Act applies only to sports betting, not other types of gaming (*In re MasterCard Int'l Inc.*, 2002). This court's opinion upheld the ruling of a lower federal court in Louisiana, which found "sporting" modifies both "event" and "contest," and, therefore, the federal Court of Appeals concluded the Wire Act alone does not prohibit betting on Internet casino games.

Nevertheless, courts in other federal circuits have drawn different conclusions, finding the second and third prohibited uses of a wire communication facility under Subsection 1084(a) (i.e., transmitting information assisting in placing bets and transmitting entitlement to receive money or credit resulting from a bet) do not require that the bets to which those prohibited uses relate be limited to bets placed on sports alone.

In *United States v. Lombardo*, the federal court concluded the phrase "sporting event or contest" modifies only the first of the three prohibited uses of a wire communication facility (i.e., transmitting bets) (*United States v. Lombardo*, Memorandum Decision and Order Denying Defendants' Motions to Dismiss, 2007). The court continued, finding that Congress must have intentionally excluded "sporting event or contest" as a qualifier from the second and third prohibited uses and thus indicates that at least part of Subsection 1084(a) applies to forms of gaming that are unrelated to sporting events. In reaching this decision, however, this federal court inexplicably cited

a state court decision indirectly supporting its conclusion that the Wire Act applies to gaming other than sports betting. Based on the manner in which the US legal system functions, as described earlier, this is problematic for several reasons. First, a federal court is relying on a state court's interpretation of a federal law when the federal court should interpret the federal law—not look to a state court's interpretation of federal law for the basis of its interpretation. Second, if a federal court is going to look to another court, then it should have looked to prior federal court decisions on the same subject matter, like the ruling of the Fifth Circuit court just mentioned. Third, even if a basis existed to rely on the state court, the federal court's reliance was in error since the state court did not even actually address the issues underlying the federal court's conclusion.

Recently, another court used comparable logic, finding the Wire Act applicable to nonsports betting and thus denied a motion filed by Gary Kaplan⁸ to dismiss the Wire Act counts charged against him (*United States v. Kaplan*, 2008). Although the *Lombardo* court and the *Kaplan* court each find the Wire Act applicable to all types of gaming, even they did not uniformly comprehend the Wire Act's language since they reached their conclusions by interpreting Subsection 1084(a) differently (Hichar, 2009).

An analysis of the Wire Act's legislative history and the exceptions in Subsection 1084(b) along with the prohibitions in Subsection 1084(a) substantiate that the positions of the *Lombardo* and *Kaplan* courts are nonsensical. To contend Congress was more concerned with nonsports betting, such as betting on lotteries and casino games, than with betting on sports events is not justifiable (Hichar, 2009). For instance, even the title of the House Judiciary Report on the legislative bill that became the Wire Act was entitled "Sporting Events—Transmissions of Bets, Wagers, and Related Information" (H.R. Rep. 87-967, 1961). Additionally in 1961 when the Wire Act was enacted, the notion that a person would use the telephone or telegraph

to bet on anything but race and sporting events was unrealistic (*In re MasterCard Int'l Inc.*, 2002). Consequently, the prohibitions in Subsection 1084(a), like the safe harbor in Subsection 1084(b), were likely intended to apply only when the underlying betting related to sporting events or (sporting) contests.

The Interstate Horseracing Act

Even if courts, unlike the *Lombardo* and *Kaplan* courts, strictly follow the legislative history and wording of the Wire Act and do not make efforts to expand the applicability of the Wire Act's language, questions still arise as to the ambit of the Wire Act. Most notably, does the Wire Act's general prohibition apply to interstate or foreign betting on the sport of horseracing? While one may question the veracity of such a concern given the relative straightforwardness of sports betting as the basis for the Wire Act, ambiguity has arisen from the differing viewpoints between the horseracing industry and the DOJ.

As discussed, the Wire Act prohibits "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. . . ." (Federal Wire Wager Act of 1961, 2009), whereas the safe harbor provision excepts from the general prohibition "the transmission in interstate or foreign commerce . . . of information assisting in the placing of bets or wagers on a sporting event or contest from a State or foreign country where betting on that sporting event or contest is legal into a State or foreign country in which betting is legal" (Federal Wire Wager Act of 1961, 2009). The substantial difference between the body of the Wire Act and the safe harbor is that the Wire Act makes it unlawful to transmit bets, information assisting in the placing of bets, and information entitling persons to money or credit resulting from bets, while the safe

harbor only excepts the *interstate or foreign transmission of information assisting in the placing of bets*.

This seemingly small difference opened the door for the horseracing industry to allow innovative betting methods on an interstate and foreign platform, particularly off-track betting. Besides accepting bets directly at the racetrack, US racetracks also accept off-track betting on horseraces, which, in general, is any system enabling patrons to place bets on races while not being physically present at the racetrack and usually is done through an intermediary. The two most prevalent forms of off-track betting are account wagering (also known as advance deposit wagering) and off-track betting facilities (also known as OTB facilities). Account wagering allows a patron to make advanced deposits with an intermediary or the racetrack and then place a bet via the telephone, computer, or other method of communication. An OTB facility, on the other hand, is a physical location where patrons assemble to place bets on the races being conducted at another location.

The Interstate Horseracing Act (IHA) was enacted in 1978 and provides rules to govern the horseracing industry and off-track betting conducted on an interstate basis. Specifically, the IHA was enacted "to regulate interstate commerce with respect to wagering on horseracing in order to further the horseracing and legal off-track betting industries in the United States" (15 USC § 3001(b)). The states and the horseracing industry viewed this enactment as buttressing the legality of their off-track betting, which existed prior to the IHA's enactment (Cabot, 2010; Penchina, 2006). This was until 1999, when a DOJ representative announced that the IHA "does not allow [interstate bets on horseracing], and if a parimutuel wagering business currently transmits or receives interstate bets or wagers (as opposed to intrastate bets or wagers on the outcome of a race occurring in another state), it is violating federal gambling laws" (Hearings on House Bill 3125, 2000; Jennings, 1999). As a consequence, the horseracing interests sought clarification of

the law through an amendment to the IHA (Cabot & Christiansen, 2005).

The IHA was amended in 2000 to specifically clarify that pari-mutuel horserace betting may be conducted on an interstate basis, which includes placing bets that are lawful in each state involved and accepted by an off-track betting system in such states by telephone or other electronic media (i.e., the Internet).⁹ (The IHA as amended only addressed interstate pari-mutuel horserace betting; foreign and other bets will be discussed later.) (Interstate Horse Racing Act, § 3002(3), 1978).

However, in the 2001 *Cohen* case discussed earlier, the argument that sports betting fell within the Wire Act's safe harbor was rejected (*United States v. Cohen*, 2001). Specifically, Cohen appealed the district court's instructions to the jury regarding what constitutes a bet per se. Cohen unsuccessfully argued that the WSE operations fell within the safe harbor because under WSE's betting system, which Cohen likened to horserace account wagering, the transmissions between WSE and its patrons contained only information that enabled WSE itself to place bets from patron accounts located in Antigua (*United States v. Cohen*, Appellant's Brief, 2000, pp. 2, 8, 16–20).

Although Cohen lost his argument, horseracing interests have a major point of distinction between their position and the Cohen facts—namely, the IHA. The fact that the IHA was enacted 16 years after the Wire Act and then later amended for clarification goes toward finding congressional recognition of the legality of interstate off-track betting on horses and specific congressional intent to except horseracing and its associated interstate betting from the Wire Act's prohibitions.

Another distinction between the IHA and Cohen is the safe harbor provision, which requires the transfer of information assisting in placing bets must be to and from a jurisdiction in which the betting is legal (Federal Wire Wager Act of 1961, 2009). Simply, it was irrelevant how Cohen and WSE structured the sports betting transactions in

light of the fact that sports betting (not including horse betting) is illegal in New York (New York State, 1984; New York State Law, 2010a). In contrast, horserace betting is legal in New York and many other states (New York State Law, 2010b, 2010c; OfficialUSA.com, n.d.).

Nevertheless, the DOJ remains resolute in its belief that all interstate and foreign gaming is unlawful under the federal law and therefore maintains its blanket opposition to the gaming industry. In 2006, the DOJ expressed at another congressional hearing that interstate horserace betting is prohibited by federal anti-gaming laws—regardless of the IHA (District of Columbia Appropriations Act of 2001; Hearings on House Bill 4777, 2006).

This position is unsustainable. One of the greatest arguments against the DOJ's position is the recognized rules of statutory construction in the United States—those rules used to interpret laws, which alone should be a sufficient basis to defeat the DOJ's position (Kim, 2008). They state that a presumption exists that Congress is aware of existing law when it passes legislation and amends existing statutes (*In re Dobbins*, 1968; *South Dakota v. Yankton*, 1998; Singer & Singer, 2001, § 51.02, p. 194). Thus, to the extent statutes on a subject conflict, the more recent enactment will usually prevail, which is the IHA (*Marschall v. City of Carson*, 1970).

Although it's clear Congress's enactment of the IHA and its amendment was intended to legalize (and clarify the legality of) off-track betting on horses, certain inconsistencies remain that cause confusion. One, the IHA's language, as amended, is narrower than intended and only covers interstate *parimutuel* betting on horses, whereas the Wire Act does not discriminate between the types of bets that fall within the safe harbor.

Two, the IHA as amended only addresses *interstate* pari-mutuel betting, those bets “transmitted by an individual in one State via telephone or other electronic media and accepted by an off-track betting system in the same or another State,” whereas the Wire Act safe harbor excepts interstate and foreign

betting, those bets “from a State or foreign country where betting on that sporting event or contest is legal into a State or foreign country in which betting is legal.”

Even though the IHA’s amended language is narrower than the Wire Act’s language, the amended IHA should not be interpreted as legislative intent that foreign and non-pari-mutuel bets were not intended to be covered by the safe harbor (Cabot & Christiansen, 2005). As Cabot and Christiansen (2005, p. 205) note, “The better and more likely interpretation is that Congress was concerned that the [US legal stance] was infringing upon a longtime accepted and economically important activity [(i.e., interstate off-track betting on horses)] and Congress wanted to stress that the [safe harbor] applied to this specific set of circumstances” (Cabot & Christiansen, 2005). Therefore, it is not that Congress intended to allow interstate horserace betting while prohibiting foreign betting but rather Congress was addressing a specific legal issue within the United States brought by a specific lobbying group representing US horseracing interests. In doing so, Congress had not drafted the IHA and the amended IHA language to ensure it matches the Wire Act’s safe harbor language for foreign betting.

Unfortunately, these inconsistencies and the confusion surrounding US anti-gaming laws carried over to the recent dispute at the WTO. The WTO Dispute Panel, as illustrated in the section that follows, found the amended IHA language narrower than the Wire Act’s language and based on that found discrimination between domestic and foreign suppliers of remote betting services.

World Trade Organization, US—Gambling

Antigua and Barbuda (“Antigua”) argued before the WTO Dispute Settlement Body and Appellate Body that the US position on Internet gaming was inconsistent with its WTO commitments under the General Agreement on Trade in Services (GATS; World Trade Organization, 2005). Although Antigua’s argument cited numerous US federal and state laws and government

actions and statements as proof of the inconsistency, the Appellate Body ultimately rested its decision on the IHA, finding the US enforcement of the IHA was inconsistent with its GATS commitments (World Trade Organization, 2005, n.d., paragraphs 373–374). In particular, the Appellate Body issued a final report on April 7, 2005, finding the United States failed to disprove Antigua’s claim that the IHA discriminated between foreign and domestic suppliers of “remote” horserace betting services (e.g., pari-mutuel pooling and account wagering) because the IHA’s language only excepted interstate betting from the Wire Act’s prohibitions. As a result, the WTO required the United States to bring its laws into compliance with the final report (World Trade Organization, 2005, n.d., paragraphs 373–374).¹⁰ However, in fact, as discussed earlier, the Appellate Body should have found that no inconsistency or discrimination against foreign suppliers exists for remote horserace betting.

The WTO did not reach this conclusion. This is, in part, a result of both the United States and Antigua arguing inaccurate interpretations of US law. The United States, despite not being defensible, maintained the consistent position that the Wire Act prohibited all types of interstate or foreign gaming, including betting on horseracing regardless of the IHA. In contrast, Antigua argued that the IHA, “on its face, authorizes domestic . . . suppliers, but not foreign . . . suppliers, to offer remote betting services in relation to certain horse races” (i.e., because the IHA only refers to interstate and does not refer to foreign, whereas the Wire Act’s prohibitions and safe harbor cover both) (World Trade Organization, 2005, n.d., paragraphs 361–364, 371–372). Per Antigua’s view, “the IHA ‘exempts’ [US] suppliers from the prohibitions of the Wire Act” and other federal anti-gaming laws (see note 13) while prohibiting foreign suppliers (World Trade Organization, 2005, n.d., paragraphs 361–364, 371–372).

Consequently, the interests of both parties prevented them from arguing the correct interpretation of the legal landscape, which is

that both domestic and foreign suppliers of remote betting services for horseracing fall within the Wire Act's safe harbor. To argue that position would have meant the United States acknowledged the Wire Act did not prohibit all forms of interstate or foreign gaming. This is an acknowledgment the United States will not make because doing so would be contrary to the DOJ's previously described continued stance of blanket opposition to interstate and foreign gaming. If Antigua argued the correct interpretation, Antigua would be acknowledging that it suffered no discrimination, because Antigua's remote suppliers would have come under the purview of the safe harbor. In essence, the correct analysis of the law was lost because such argument and interpretation would have failed to benefit either party's case before the WTO.

In actuality, "all [remote] horserace wagering activity, whether parimutuel or not, or whether it is interstate or foreign, must fit within the safe harbor provision of the Wire Act. The Wire Act makes no distinction between parimutuel and non-parimutuel wagers and specifically covers both interstate and foreign wagering activities. Therefore, the legal analysis of foreign wagers and nonparimutuel wagers should be no different than interstate parimutuel off-track wagers" (Cabot & Christiansen, 2005). This is readily apparent when analyzing the Wire Act's safe harbor, which is the umbrella under which legal off-track horserace betting exists. Since the safe harbor does not qualify the types of horserace betting that may occur legally, any type of off-track horserace betting is legal, regardless of whether the horserace bet is pari-mutuel or not and regardless of whether the horserace bet is made on an interstate or foreign basis.

In summation, the IHA and its amendment were intended to provide further support of the legality of horserace betting. The fact that the IHA as amended discusses interstate parimutuel betting should not serve as a basis for finding Congress did not intend foreign and non-pari-mutuel bets to be covered by the Wire Act safe harbor (Cabot & Christiansen,

2005). Rather, all remote horserace betting activity, whether it is interstate or foreign, fits under the safe harbor because the Wire Act safe harbor equally protects domestic and foreign suppliers of remote horserace betting services. Thus, if the laws of both jurisdictions permit such activity, no basis should exist for prosecuting a person who *transmits* horserace betting *information* through interstate or foreign commerce.

While the IHA focuses squarely on the sport of horseracing, the Professional and Amateur Sports Protection Act of 1992, in contrast, was intended to encompass and regulate betting on almost every other amateur, collegiate, and professional sport.

Professional and Amateur Sports Protection Act

For some time, the professional sports leagues have distanced themselves from sports wagering by adopting stringent rules regarding gambling and gamblers (Cabot, 1998, p. 164). These policies stemmed from several high-profile scandals in Major League Baseball. The first and most extensive scandal broke out in 1920, when eight members of the Chicago White Sox, including its greatest star, Shoeless Joe Jackson, were accused of intentionally losing the World Series. In what would become known as the "Black Sox Scandal," all eight players were acquitted of criminal charges. Nevertheless, Kenesaw Mountain Landis, baseball commissioner and former judge, banned all eight players from professional baseball for life (Cabot, 1998, pp. 163–164). Consequently, the league adopted policies that "included bans on wagering by players, other personnel and owners, prohibitions on dual ownership of baseball clubs and legal gambling operations, and restricting professional teams from advertising or associating with legal gambling enterprises" (Cabot, 1998, pp. 163–164).

Yet even with these safeguards in place and the Wire Act's ban on interstate and foreign sports betting, the sports leagues faced a new challenge in the 1970s from an unlikely source—state governments. While only Nevada had an open sports betting industry

in the 1970s, other states began to look at tying their lottery products to professional sports (Hearings on S. 474, 1991). The innovator in these sports lotteries was the state of Delaware (Cabot, 1998, p. 164). In 1976, it introduced a “scoreboard” lottery, which, in essence, was a three-way parlay card bet on the National Football League (NFL).¹¹ Subsequently, the states of Oregon and Montana legalized similar sports-related lotteries. Then 13 other states began considering legalizing some form of sports betting.

Amateur and professional sports leagues perceived this as a threat to them for numerous reasons, including possible cheating in sports and scandals that would tarnish their image. In turn, they sought to curb state-sponsored expansion of sports betting by lobbying Congress, which ultimately resulted in the enactment of the Professional and Amateur Sports Protection Act of 1992 (PASPA). PASPA makes it unlawful for “a governmental entity¹² to sponsor, operate, advertise, promote, license, or authorize by law or compact, or a person to sponsor, operate, advertise, or promote . . . a lottery, sweepstakes, or other betting, gambling, or wagering scheme based, directly or indirectly . . . on one or more competitive games in which amateur or professional athletes participate, or are intended to participate, or on one or more performances of such athletes in such games” (Professional and Amateur Sports Protection Act, 1992).

PASPA focuses on state-sponsored sports betting, because legal state-sponsored sports betting was deemed the most objectionable and created the perception that the government approved of betting on sporting events (Hearings on S. 474, 1991). Nonetheless, PASPA did contain certain exceptions. PASPA specifically excepts (1) animal racing and jai alai and (2) sports betting operations that already were permitted under state law but only in the form in which they existed at any time during the period of January 1, 1976, to August 31, 1990. This later exception “effectively served as a grandfather clause for the licensed

sportsbooks in Nevada, the sports lottery being conducted in Oregon, a sports lottery authorized under Delaware law, and certain sports pool betting previously authorized under Montana law” (Minke & Waddell, 2008).

Of these states, Delaware garnered recent attention by attempting to reinstitute its sports lottery after a several-decade hiatus and concurrently attempting to expand the forms of sports betting allowed in Delaware (Millman, 2009). In May 2009, Delaware Governor Jack Markell attempted to implement a sports betting scheme that would include bets “in which the winners are determined based on the outcome of any professional or collegiate sporting event, including racing, held within or without the State, but excluding collegiate sporting events that involve a Delaware college or university, and amateur or professional sporting events that involve a Delaware team” (*OFC Commissioner Baseball, et al. v. Jack A. Markell et al.*, 2009, p. 5).

Soon after, however, the amateur, collegiate, and professional sports leagues filed a complaint against Delaware claiming Delaware’s plan to expand sports betting, including permitting single-game bets on a variety of sports, violated PASPA (Fromer, 2009; *OFC Commissioner Baseball et al. v. Jack A. Markell et al.*, 2009). The court concluded that Delaware is permitted to conduct sports betting “to the extent” that such a lottery or scheme was “*actually conducted*” by Delaware during the 1976–1990 time period specified in PASPA (*OFC Commissioner Baseball et al. v. Jack A. Markell et al.*, 2009, p. 21).

Accordingly, the court concluded that Delaware may institute parlay betting on at least three NFL games, which is the only form of betting Delaware conducted during that specific PASPA time period. The court found it undisputed that no single-game betting was “conducted” by Delaware during that time period to qualify for the PASPA exception (*National Football League v. Governor of the State of Delaware*, 1977, p. 1385), so single-game betting is therefore beyond the scope of the exception in PASPA and “any effort by

Delaware to allow wagering on athletic contests involving sports beyond the NFL would violate PASPA" (*OFC Commissioner Baseball et al. v. Jack A. Markell et al.*, 2009, p. 28).

Delaware is not, however, the only challenge to PASPA. Given the current economic downturn, many states now are seeking new ways to raise revenue. By way of an example, a New Jersey legislator filed a lawsuit in March 2010 seeking to overturn PASPA, arguing PASPA is unconstitutional because it treats four states differently than the other states (Gambling911.com, 2010). However, US District Judge Garrett Brown said New Jersey Senate President Stephen Sweeney, New Jersey Senator Raymond Lesniak, and the gaming advocates who filed the complaint lacked standing to challenge PASPA's constitutionality (*Interactive Media Entm't & Gaming Ass'n v. Holder*, 2011, pp. 17–19). Deciding they had no "standing" to bring the case, Brown declined to rule on their other arguments, alleging that PASPA violates the federal Constitution (*Interactive Media Entm't & Gaming Ass'n v. Holder*, 2011, p. 23). Brown concluded that under New Jersey law "the proper party to bring such a claim would be New Jersey's attorney general, but the governor and attorney general have not intervened in this lawsuit" (*Interactive Media Entm't & Gaming Ass'n v. Holder*, 2011, pp. 30–31). Nevertheless, in his decision to dismiss, Brown left the door open for future efforts to overturn the unconstitutional ban in the courts. Specifically, if voters in New Jersey approve a referendum that will be on the ballot this November to allow the New Jersey legislature to authorize by law sports betting at Atlantic City's casinos and the state's horse tracks, New Jersey's governor and attorney general may feel compelled to reinstitute the lawsuit. Additionally, Iowa, Missouri, and Rhode Island also are looking to legalize sports betting despite the existing federal prohibitions and are putting Congress on notice that they would like the prohibitions lifted (Jacobs, 2010; Missouri House Concurrent Resolution of 2010, 2010; Szyba, 2006). But for the time being, PASPA permits

only Nevada, Oregon, Delaware, and Montana to offer state-sponsored sports betting and only as that betting was conducted prior to PASPA's enactment.

Unlawful Internet Gambling Enforcement Act

Another recently enacted law intended to restrict gaming in the United States is the Unlawful Internet Gambling Enforcement Act of 2006 (UIGEA), which Congress passed on September 29, 2006. UIGEA created a new federal criminal offense imposed primarily against Internet gaming operators offering traditional gambling games and accepting financial payments (i.e., deposits for game play) in support of their "unlawful Internet gambling." UIGEA provides that no person engaged in the business of betting or wagering may knowingly accept most payments, including credit, the proceeds of credit, credit card payments, electronic fund transfers (EFTs), or the proceeds from EFTs, checks, drafts, or similar instruments, or the proceeds from any other financial transaction from a player in connection with unlawful Internet gambling (Unlawful Internet Gambling Enforcement Act, 2006). In other words, UIGEA seeks to cut off the flow of funds from US gamblers to Internet casinos.

UIGEA defines "unlawful Internet gambling" as "to place, receive, or otherwise knowingly transmit a bet or wager by any means which involves the use, at least in part, of the Internet *where such bet or wager is unlawful under any applicable Federal or state law* in the state in which the bet or wager is initiated, received, or otherwise made" (Unlawful Internet Gambling Enforcement Act, 2006). This appears identical to the existing law under the Travel Act and the Illegal Gambling Business Act¹³ where federal prosecutors need to show a violation of another law to be a violation of these Acts. The words of UIGEA, however, are more favorable to the prosecution, because UIGEA only requires the prosecution to prove that a bet on a game is illegal under state law, which is a much easier threshold to surmount than proving the Internet gaming operator violated a state or federal law.

For example, some states make it unlawful for persons to play poker for money. These statutes would not directly assess liability on a poker site because they are not players. The bets, however, are unlawful under state law. Therefore, the site may be charged under UIGEA for accepting the financial transfer even if it did not violate the state law directly. That is, an act not done by the Internet gaming operator is sufficient to hold the operator in violation of UIGEA. By way of another example, Internet gaming operations accepting bets on a game of basketball or football would violate UIGEA in the states that have specifically made such betting illegal, and even in those states without such laws, UIGEA would be violated since federal laws (discussed earlier) prohibit such betting.

UIGEA's prohibitions do not extend to all portions of the gaming industry. UIGEA does not apply to interstate horseracing that complies with the IHA, fantasy sports or simulation sports games, games and contests that do not require consideration other than personal efforts to play or obtain Internet access, and educational games or contests. Of course, these exclusions would not apply to the acceptance of bets from patrons from states where betting on these excluded games is not permitted under a state's law. Thus, Internet gaming operators must consult state gaming laws—much like some of the other federal laws—to determine the extent to which their activities may violate UIGEA, fall within the US legal framework, or require modifications to fall within the legal framework.

State Laws

As discussed, federal gaming law does not outright prohibit all gaming transactions. Rather, federal gaming law generally only prohibits certain forms of participation in gaming transactions where the transactions are in violation of state law in the state where they occur, subject to any federal law constraints on the states. This is consistent with the underlying federal policy to assist the states in the enforcement of their respective state gaming laws. By specifically

requiring a predicate state law violation, all doubt is removed as to the ability of the states to set their own gaming policies and look to federal laws for assistance in doing so. Thus, in order to address the potential scope and applicability of the federal law and to determine if a form of sports gaming is legal, one must look to the individual state laws.

Each state has the power to adopt its own versions of laws and, just like federal law, state laws are constantly being amended and repealed. Consequently, the laws governing the various gaming subcategories often are inconsistent between the states. Nevertheless, most states do have some commonality in their general approach to gaming. Prohibited gaming generally involves any activity in which the following elements are present: (1) the award of a prize, (2) determined on the basis of chance, and (3) where consideration is required to be paid. If any of these three elements are missing, then the activity is generally allowed under state law (Cabot, Light, & Rutledge, 2009).

Currently, many forms of sports gaming activities can fall within the US federal and state legal framework; perhaps one of the most thriving activities is fantasy sports. Several reputable operators offer fantasy sports contests based on the theoretical premise that fantasy sports are competitions between the fantasy "team owners" who draft players to their teams, and these fantasy team competitions are independent of the actual skill of the athletes or performance of the sports teams. The winners of the competition are based on the accumulated statistics of individual athlete performances in particular sports, such as batting average in baseball or yards gained in football (Isidore, 2006). The key to the distinction between fantasy sports and sports betting is that fantasy sports require the consistent and recognizable involvement of the contestants to the point of complete immersion in the contest and to achieve success such that the activity transforms from something outside their control to something within their control (Cabot & Csoka, 2007). Some of the larger fantasy sports websites are operated by CBS,

ESPN, FOX, and Yahoo! (e.g., CBSSports.com, ESPN, Fox Sports, Sporting News, and Yahoo! Sports).

Of course, many other sections of the sports gaming industry are available for business opportunities. It seems businesses are continually developing new Internet-based gaming products for consumers (Levy & Satariano, 2009). Additionally, over 100 horserace tracks operate in the United States, and some of these also are racino operations with slot machines (OfficialUSA.com, n.d.). Disseminators of sports and race information, live broadcasts and simulcasts, touts, and handicappers also play a significant role in the sports gaming industry (e.g., Betting Kings, Daily Racing Form, NBA Choice). Off-track betting services also are prominent portions of the sports gaming industry in the United States (e.g., Allhorseracing.com, Capital Off Track Betting, Illinois OTB, TVG). All of these various gaming opportunities are grounded in the state laws of the states in which they exist. This is why it is necessary to vet a proposed gaming activity by conducting an analysis of the state laws applicable to where the activity would occur. While labor-intensive and costly, there is no other way to assess a gaming business's risk without surveying each state in which the game or service will be offered. These surveys are key to assessing potential state violations that serve as the basis for the ominous federal violations discussed earlier by categorizing the risk associated with offering a proposed gaming model to persons physically located in each state. This enables a company to review the results of the survey, assess the risk posed by each state's law, and decide those states in which it will operate.

Conclusion

The billions of dollars in revenue generated by the US sports gaming industry is sufficient evidence of the plentiful sports gaming business opportunities that exist. As noted, these opportunities range from traditional bookmaking activities, such as those in Nevada, and pari-mutuel race activities, such as those conducted across the

United States, to involvement in the most recent sports-derived game innovations, such as fantasy sports, skill game contests, and Internet-based games. However, due to the complex and intricate US legal framework, it is key to vet the proposed sports gaming business by conferring with counsel regarding a thorough review of the proposed business and analysis of the applicable state and federal law prior to entering the US market. This practice assists operators in assessing legality and making educated choices as to the level of risk they wish to hold or the necessity of modifying the business model.

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Notes

¹ This article was written in June 2011 and published in the *Thunderbird International Business Review*, © 2011 Wiley Periodicals, Inc

² The terms *bet*, *wager*, and their derivatives are essentially synonyms for the same activity. For consistency, *bet* is used in this review unless another term reflects standard industry use or is expressly used by the source reference.

³ All dollar amounts referred to herein are in US dollars.

⁴ With regard to state laws, most states have some commonality in their general approach to gaming. Prohibited gaming involves any activity in which a person pays consideration—usually cash—for the opportunity to win a prize in a game of chance. As a consequence, if any of these three elements are missing, then the activity is

generally allowed under both state and federal law. Currently, 48 states and the District of Columbia allow some type of traditional gambling activity, while only Utah and Hawaii restrict all forms.

⁵ For consistency, the following terminology will be used in this article as it is used in US law. The term *intrastate* refers to transactions wholly within a US state or territory, the term *interstate* refers to a transaction between two or more US states or US territories, the term *foreign* refers to transactions between a US state or US territory and another country, and *foreign jurisdiction* refers to a jurisdiction other than a US state or territory.

⁶ The language of the statute “wire communication facility” refers to the technology that existed at the time of enactment—namely, telephone and telegraph communications (Federal Wire Wager Act of 1961, 2009). However, this term has been interpreted to encompass almost any known communications medium, including the Internet.

⁷ In *United States v. Barborian* (1981, p. 328), the federal district court quoted from the 107 Cong. Rec. 16,534 (1961) and concluded that Congress did not intend to include social bettors within the umbrella of the statute, even those bettors that bet large sums of money and show a certain degree of sophistication.

⁸ Gary Kaplan is a founder of the Internet gaming website BetOnSports.com, a website that was the world’s largest Internet sportsbook. BetOnSports was based in Costa Rica and accepted bets from people located across the globe. In 2004 alone, BetOnSports had a million registered customers and accepted more than 10 million sports bets in excess of a billion dollars (“BetOnSports Finds \$28 Million,” 2009; *United States v. Kaplan*, 2008).

⁹ Despite what was an unequivocal pronouncement that account wagering was legal pursuant to the IHA amendment, the DOJ still will not concede the legality of off-track betting. In a press statement signing the IHA amendment into law, President Clinton commented that the DOJ continued its position on “common pool wagering and interstate account wagering” (Clinton, 2000).

¹⁰ The United States did not comply with the WTO Dispute Panel ruling, so Antigua and Barbuda received WTO authorization to impose remedial trade sections of \$21 million annually (World Trade Organization, n.d.). Ultimately, the United States withdrew its (WTO Dispute Panel–found) commitments to gambling under GATS and has begun negotiations of compensation adjustments for certain WTO members (Office of the United States Trade Representative, n.d.).

¹¹ A parlay is a bet placed on the outcome of two or more events in which the bettor must have correctly chosen each event’s outcome to win. An example of parlay betting is selecting the winning basketball team in three different games. All three teams selected by the bettor must win for the bettor to win.

¹² The term *governmental entity* is defined to mean any US state, territory, Native American tribe, or any subdivision of these entities (Professional and Amateur Sports Protection Act, 1992).

¹³ Neither the Travel Act nor the Illegal Gambling Business Act is violated unless another law is first violated. Both also can potentially apply to sports betting, on and off the Internet.

The Travel Act of 1961 (2009) prohibits any person from using “any facility in interstate or foreign commerce” (e.g., credit cards, bank teller machines, FedEx, telephone, etc.) with the intent to promote, manage, establish, carry on, or facilitate unlawful activity. Unlawful activity is defined as “any business enterprise involving gambling” in violation of state or federal laws. Therefore, a person using a facility in interstate or foreign commerce for an activity deemed to be in violation of state or federal gaming laws could be simultaneously deemed to violate the Travel Act.

The Illegal Gambling Business Act of 1970 (2009) prohibits any person from financing, owning, or operating an illegal gambling business. An illegal gambling business is defined as an operation that violates state law, involves five or more persons, and either is in substantially continuous operation for more than 30 days or has a gross revenue of more than \$2,000 in any single day. Under the Illegal Gambling Business Act, essentially anyone who participates in an illegal gambling business, other than a mere bettor, may be subject to criminal liability under federal law.