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Internet Gambling

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It has been said that Australians would bet on two flies crawling up a wall. If that is so, the advent of the digital age will further enhance gambling opportunities. Today, anyone with a personal computer and modem has their own personal casino. In addition to virtual casinos, the online sports betting industry and online lotteries have begun to proliferate, in Australia and throughout the world. These developments pose significant challenges and opportunities.

In 1997, the Australian Institute of Criminology, in partnership with the Australian Institute for Gambling Research, convened a roundtable on electronic gambling which set the stage for a national conference held in May 1998. The following pages highlight some of the major themes covered in these two events.

Discussions of gambling in general, and of Internet gambling in particular, tend to generate more heat than light. This Trends and Issues essay is a notable exception, and will go a long way towards redressing this imbalance.

It explores the proliferation of Internet gambling, its potential benefits, and its downside risks. The paper is intended to inform policy makers and members of the public about rapid developments in gambling technology so that these developments may be managed in the best interests of all Australians.

Adam Graycar
Director

Australia has entered the digital age. The convergence of computing and communications is already changing the way we live. Health, education, banking, indeed every institution in society, is undergoing profound change as the result of new technologies. This is no less the case with gambling.

Gambling has been part of Australian culture since the arrival of the First Fleet. In most of its forms, gambling can be an exciting way to spend one's spare time, and one's spare money. Today, it is an important industry in its own right, employing thousands of Australians, and greatly enhancing Australia's reputation as a tourist destination. It has also become an important source of revenue for Australian States and Territories.

On the other hand, there are those who have argued that Australians already have too many opportunities to gamble, and that some of us bear too many burdens as a result. Recent inquiries established by Commonwealth and New South Wales Governments, and the election to the Parliament of South Australia of a single-issue candidate strongly opposed to gaming machines, suggest a heightening degree of concern about the costs and benefits of gambling in Australia today.

These concerns arise primarily from the conduct of gambling in its traditional forms. But technology has begun to change the face of gambling no less than it is changing the way we work, the way we study, and the way we do our banking. Most importantly, the advent of Internet gambling has brought about a proliferation of gambling opportunities which were previously unimaginable.

This paper highlights some of the key regulatory issues and policy debates which have arisen for governments, operators and

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the community since the recent advent of interactive and Internet gambling. Rather than recommending any definitive solutions, it raises questions about the implications of new technology and gambling for Australian society, and urges a consistent national approach to the issue.

Gambling in the Digital Age

Today, anyone with a personal computer and a modem can access Internet gambling sites in Australia and around the world. A quick web search with any standard search engine using the term "Internet Gambling" will yield an abundance of gambling sites, through which one can play a variety of games such as blackjack, baccarat, and roulette, as well as wager on the outcome of sporting contests and participate in lottery draws. In only a matter of months, with the advent of interactive television, the potential will exist for any Australian to have all these forms of gambling in their home.

The emerging interactive gambling industry has demonstrated the enormous commercial potential of new technologies. Estimates of the potential market for online gambling services vary widely, but there is little doubt that it could entail billions of dollars annually by the turn of the century. Notwithstanding the current Asian economic crisis, there are tremendous profits which await those entrepreneurs who can meet the gambling demands of the emerging Asian middle class, whose own governments may discourage gambling on their own soil. Similar market opportunities exist in America and Europe.

But for all its attraction as a means of recreation, entertainment and export earnings,

gambling may entail societal risks which we should seek to manage. Many of these risks are common to gambling in any form, while others are enhanced by digital technology.

What can go wrong with Internet gambling?

First, there are the downside consequences of gambling in any form:

- The risk that a small number of gamblers experience problems with their gambling or are unable to control their impulse to gamble. This may lead to diminished job performance; increased family stress; fraud or theft in order to pay one's gambling debts; indeed, financial ruin. It may also invite "loan sharking" — extortionate lending practices.
- Gambling on sporting events can lead to corruption, as those with a vested interest in the outcome of a match might offer inducements to one or more players to underperform.
- Preliminary research shows that gambling is regressive in its impact. It weighs most heavily on those who are least able to afford it.

Then, there are those negative aspects of gambling which are perhaps more salient in the digital age:

- A gambling site on the other side of the world may or may not be legitimate. There may be very little to prevent the provider of online gambling services from taking one's money and shutting down, or failing to pay winnings. Without the protection of government licensing and regulation, the loser has very little recourse.
- Credit card or account details may be vulnerable to capture, and funds vulnerable to theft by computer hackers.

- Online gambling facilities could be used as vehicles for money laundering, where the proceeds of crime may be disguised as winnings.
- Online gambling facilities may be accessible by children.
- Internet gambling may be vulnerable to invasions of privacy. Information given to casino operators can be used for other purposes. For example, a "tout" service that uses telemarketing to convince people to bet on its football betting system may be willing to pay money for a list of Internet sportsbook players.
- Online activity, which appears addictive in its own right for a minority of users, may interact synergistically with the propensity for problem gambling, and thereby increase the number of problem gamblers or the intensity of their problems.

An expansion of gambling opportunities provided by Internet technology may well stimulate a growing demand for gambling services. All else being equal, the risk of each of the problems outlined above will be that much greater.

The global nature of cyberspace, which knows no geographic boundaries, means that one can sit in one's bedroom in Melbourne and gamble at a virtual casino whose server is located on an island in the Caribbean. Not only does this eclipse any notion of community control which characterised traditional gambling of years past, it poses particular problems for taxation authorities, and jeopardises the revenue base of those Australian States and Territories which have depended on gambling as a source of funds.

The advent of Internet gambling may also expect to impact on other forms of gaming and wagering. Just as the advent

of casino gambling in Australia came at some expense to the racing industry, so too may “cyber” gambling reduce the income of “location based” gambling industries, with detrimental consequences for employment in hotels and clubs. Precisely which segments of the industry will win or lose, and by how much, remains one of the big unanswered questions as gambling proceeds through the digital age.

One may thus anticipate a degree of instability in the gambling industry both in Australia and around the world. This may well entail restructuring in the form of mergers between sectors, such as gaming and racing operators, as well as between industries. The convergence of some gambling and telecommunications interests has already begun to appear. The impact which these trends will have on Australians’ propensity to gamble is not yet clear.

Policy Challenges

Several governments have begun to devote attention to the issues of interactive and Internet gambling.¹ The variety of options to deal with Internet gambling may be reduced to three basic strategies. The two extremes are strict prohibition of online gambling on the one hand, and a *laissez-faire*, or “do-nothing” response on the other. Between these extremes is the path of

1. *The NZ Department of Internal Affairs Review of Gaming series 5; the NZ Casino Control Authority; the NT Select Committee on Interactive Television Gaming; Parliament of South Australia Social Development Committee; Australian Regulators Working Party.* Their published reports and papers provide a summary of the current understanding of the issues among regulators. A useful background document is the *Draft Regulatory Control Model for New Forms of Interactive Home Gambling*, produced by the Australian Regulators Working Party (16 May 1997).

regulation, which seeks to strike a balance by enhancing the benefits of this emerging application of information technology, while endeavouring to minimise its downside consequences. We address each of these strategies in turn.

Strict prohibition

A policy of strict prohibition of Internet gambling would make anyone criminally liable who places or accepts a wager online. This is much easier to advocate than it is to implement. As in other areas of computer-related crime, there is a poor understanding of Internet technology on the part of those who would want to control gambling on the Internet.

Strict prohibition would be extremely difficult, if not impossible to achieve in practice. Even an attempt at strict prohibition can have unanticipated and unfavourable consequences. Attempts to prohibit Internet gambling in some overseas jurisdictions appear to have led to the displacement of the offending sites to “regulatory havens” — usually small nations with little or no regulation.

Even if one were to succeed in closing down every provider of Internet gambling services within one’s own jurisdiction, one would be hard pressed to prevent the determined gambler from “dialing” a server offshore, constrained only by the inconvenience of obtaining an external connection and by the additional telephone charges. Government efforts to inhibit Internet gambling by prohibiting related financial transactions may be defeated by services which offer to process all transactions in a permissive jurisdiction.

Here we begin to see a situation where if one jurisdiction outlaws Internet gambling, it could be forced to bear all the

costs of enforcement, while the gambling revenues continue to flow to another jurisdiction.

Despite these looming problems, prohibition is a popular solution for some, and attempts to prohibit online gambling will continue. Legislation recently introduced in the Congress of the United States would make it a crime to place or to receive an online wager, and provides for up to 6 months in prison for placing a bet online. Authorities in at least two States in the USA have sought to use consumer protection laws against online gambling sites originating outside their jurisdiction, claiming that the provision of gambling services purported to be legal actually constitutes false advertising.

Such initiatives raise the problem of extraterritorial jurisdiction and international cooperation, areas in which there remain many unanswered questions. Would the proprietor of a service operating legally from Melbourne be liable to prosecution under Minnesota law for taking bets from a player in Minneapolis? To what lengths should Australian governments go to assist foreign states in enforcing their law, when the activity in question is legal on Australian soil?

The challenge faced by those governments which seek to criminalise online gambling is made more difficult by the nature of cyberspace, which knows no physical frontiers. The degree of surveillance required to detect online illegality is often formidable. The difficulties of locating, investigating, and prosecuting an online offender who happens to be situated offshore are substantial. Law enforcement resources of most nations are limited, and the capacity of police to detect and investigate sophisticated high technology crime even more so.

Australia is no exception. While prohibition would quite likely reduce online gambling to some extent, it might detract from the capacity to address other, more pressing forms of online illegality such as fraud, child pornography, or the more serious forms of computer hacking.

And while a regime of prohibition will not suppress gambling entirely, it would certainly dissuade involvement on the part of legitimate gaming operators who would be loathe to jeopardise their land-based casino licences through involvement in prohibited activity. Prohibition might thus be expected to result in laws which are largely unenforceable, and to create a black market in online gambling services.

Laissez faire

The laissez-faire approach, by contrast, would quite possibly lead to a proliferation of gambling services, and to an increase in the demand for these services. At the same time, all of the downside consequences of online gambling would magnify and remain unaddressed. For this reason, total non-regulation of Internet gambling activity is not seriously canvassed as a policy option by most jurisdictions, although it exists by default in those developing nations whose lack of infrastructure inhibits take-up of new technologies on any significant scale for the foreseeable future.

Regulation

A regulatory strategy recognises the downside risks of online gambling and is designed to minimise them while providing every opportunity to realise upside potential. Its fundamental premises are essentially that of harm minimisation and consumer protection.

The theoretical foundation of such a strategy is not unlike that

which supports companies and securities regulation, or indeed, the regulation of “physical” casino gambling: to ensure the integrity of markets. In other words, it is suggested that a regulatory system which guarantees the probity of service providers, assures fair play, and is subject to official scrutiny, will attract business to those providers who have the highest reputation, and drive unscrupulous competitors out of business. It would conserve limited law enforcement resources for use against the worst offenders. Because legitimate government oversight brings credibility to an industry, members of the Australian Internet gambling industry welcome some form of regulation.

Australian initiatives

Initial developments in Australia suggest that the strategy favoured for the control of online gambling is the regulatory model.

On 3 May 1996, a meeting of all Australian Gaming and Racing Ministers agreed on a set of principles for a draft National Regulatory Model for new forms of interactive home gambling products.

In 1998, Queensland enacted the first major effort to legalise, license and regulate Internet gambling along the lines of the draft model. The *Interactive Gambling (Player Protection) Act*, places considerable importance on the issue of consumer protection and less on technical controls. The Northern Territory most recently has amended its gaming conduct Act and authorised the licensing of Internet gambling, but without incorporating the principles of the Draft Regulatory Model. The model currently provides for stringent integrity and probity checks and the licensing of those who would provide gambling

services, approval for each service or game to be offered, and periodic audits of gaming software.

The Draft Regulatory Model contains a number of basic principles. These include:

- Licensing of service providers pursuant to background checks and determination of financial capacity to pay out winnings
- Requirements for player authentication to prevent betting by minors
- Prohibition on credit betting
- Periodic audits of providers’ accounts and gaming software by regulatory authorities
- Required reporting of relevant transactions to AUSTRAC
- Prohibition on advertising unlicensed products
- Facilities for players to specify certain protection measures, such as self-exclusion and maximum limits on wagering
- Services to include contact information for assistance with problem gambling
- Requirements for the maintenance of privacy of player information.
- A Code of Conduct developed by industry.

Taxation to be applied based on the location of residence of the player (when in Australia), with taxes remitted to the player’s jurisdiction.

As suggested by some of the above provisions, technology may also serve as a regulatory tool. It enables computerised monitoring, auditing, and the implementation of consumer protection regulations. It would enable a player, for example, to set strict limits on the amount he or she can wager, the amount he or she can lose, and the amount of time spent in play.

In addition to those elements of the regulatory model, there are those technologies which parents and school administrators may acquire in order to block children's access to objectionable sites. Blocking and filtering software can be programmed to deny access to gambling services as well as other content specified at the discretion of the parent or teacher.

The issue now facing Australia is to determine the appropriate mix of government involvement in the regulation of gambling. The policy of the current Federal Government is to leave regulation to the States and Territories. A coherent regulatory framework, on the other hand, requires a high degree of consensus, lest revenues flow disproportionately to one State, not necessarily the one offering the best consumer protection and technical integrity. Moreover, some key issues appear beyond the power of State governments to control: for example, authority over international financial transactions, banking and telecommunications remains the constitutional power of the Commonwealth.

Regulatory models and options

The fundamental question is whether Internet and interactive gambling can be controlled, and to what extent. Most Australian regulators seem to agree that it can never be completely prohibited. Certainly the degree of control which has been achieved over site-specific gambling is not possible with cross-border gambling. But it can be controlled to a degree — and the Draft Regulatory Model indicates that Australian governments are prepared to confront the issues now with the resources available to them.

The question remains, however, whether the approach proposed in the Draft Regulatory

Model is that which is most likely to be effective. The basic principle underlying the Draft Model is one of intergovernmental cooperation and agreement. The challenge faced by State governments is to adhere to the agreed policies, standards and procedures over time, rather than succumb to interstate rivalry, pressures from local gaming operators and competition for market advantage, and then break ranks. The history of intergovernmental relations and industry policy in Australia suggests that this is very probable, sooner rather than later.

The Model also places considerable emphasis on self-regulation by gaming operators and their clients. The question remains, however, whether self-regulation is feasible, that is, whether development of standards and procedures which allow operators and citizens to make choices and regulate their own behaviour are likely to be effective with gambling.

A range of other issues also merit further consideration. The tax arrangements proposed in the Draft Regulatory Model would enable State governments to provide tax advantages to attract gaming operators to their State. Whilst this may be in the national interest, a common agreement about tax rates might be more appropriate. Currently Australian jurisdictions have widely varying tax rates, and without Federal involvement it is likely that tax inconsistencies and concessions for competitive advantage will prevail. The effects of such arrangements on fiscal policy and social welfare should not be ignored.

Conclusion

One of the key themes of government in modern times has been the extent to which the state

should protect citizens from themselves. The extent to which government should intervene in the consensual interactions of adults is an enduring issue.

We see many examples of such protection: seat belts; bicycle helmets; restrictions on the use of drugs, and consumer protection issues generally. On the other hand, the domains of gambling and consensual sexual activity have experienced a long-term trend towards the permissive. But these, certainly in their commercial manifestations, have been accompanied by a degree of regulation to protect citizens, particularly those who may be among the more vulnerable.

As far as Internet gambling is concerned, the genie is out of the bottle. Whatever actions Australian governments take, gambling opportunities will proliferate in cyberspace. By providing a basic regulatory foundation which would ensure the integrity of domestic online gambling enterprises, Australia is poised to become a world leader in the provision of online gaming services and the technologies and applications to support it. Consumers from around the world should be confident that they will get a fair deal in all Australian jurisdictions.

Australia can take the lead to foster an industry based on state of the art technology, and with a worldwide reputation for integrity. Australian policy-makers can assist Australian entrepreneurs to maximise the upside potential of the new technologies, to minimize their downside risks, and to encourage competitiveness in Australian enterprise. The fundamental questions remain

- do we know enough about the social, economic, and criminal ramifications of online betting to be able to identify them and “engineer them out”?

and

- does our political system have the capacity to develop and implement a regulatory system which would establish and maintain the high regulatory standards which have characterised Australian gambling to date?

The Draft Regulatory Model embraces the classic themes of federalism — unity within diversity. That is, formal agreement between jurisdictions on matters of principle, but allowing for diversity in application. Inevitably such an approach involves contradictions and tensions which could be reflected in the policies which evolve in the various States. Given Australia's experience of interstate competition for the local gambling market, it is difficult to see how the two principles can be reconciled with regard to cross-border gambling.

In summary, it would appear that failing the development of an adequate, coordinated response by the States and Territories of Australia, Commonwealth government involvement would be necessary if a regulatory regime is to be at all effective. The Commonwealth, of course, could prohibit Internet gambling, but would risk a State backlash as well as significant non-compliance by individuals. If Internet gambling is legalised, a national approach with common legislated standards, tax rates and operating conditions is desirable. At a more pragmatic level, the States simply do not have adequate powers to enforce regulation, or to protect consumers and licensed operators. There are three heads of power in the Australian Constitution which would permit a Commonwealth role:

- the power over telecommunications — and thus the control of telecommuni-

cations technology. This will apply whether or not Australia legalises or prohibits Internet and interactive technology;

- the power over banking and cross-jurisdictional financial transfers;
- the external affairs power. Cyberspace gambling will inevitably generate disagreements between nations on standards and legislation, and perhaps more serious international disputes.

Without Commonwealth involvement, interstate rivalry and competition may erode standards, drive down the tax benefits and expand the market with the inevitable social costs. The international reputation of Australian gambling regulation, and its impact on our society and economy, are at stake. Having said that, we are torn between two imperatives: if we are to regulate, it is important to move fast, capitalising on Australia's reputation for effective regulation and thereby achieve a global market advantage. On the other hand, a haphazard rush to regulate might result in an inferior framework, where downside risks might predominate. It would appear that Australia has only one chance to get it right.

NOTE:

Papers presented at the May 1998 Conference on Internet Gambling jointly convened by the Australian Institute of Criminology and the Australian Institute of Gambling Research will be made available on the AIC website: <http://www.aic.gov.au>

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