HARVARD UNIVERSITY
JOHN F. KENNEDY SCHOOL OF GOVERNMENT
INSTITUTE OF POLITICS

JAMES A. LEACH
DIRECTOR

79 JOHN F. KENNEDY STREET
CAMBRIDGE, MASSACHUSETTS 02138
TEL (617) 495-1363
FAX (617) 495-8957

July 28, 2008

The Hon. Ben S. Bernanke
Chairman
Board of Governors
of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

The Hon. Edward P. Lazear
Chairman
Council of Economic Advisers
The White House
1600 Pennsylvania Ave., N.W.
Washington, D.C. 20500

Dear Mr. Chairmen:

One of the issues that the Treasury and Justice Departments and the Federal Reserve System will have to address in the coming months relates to the issuance of implementing rules about a statute, the Unlawful Internet Gambling Enforcement Act (UIGEA), which is the last law I authored as a Member of Congress.

UIGEA is controversial. Concerned parties, particularly gambling interests, have lobbied assiduously in the rule making process and in the House Financial Services Committee to change the scope of the Act.

In this context, I would be appreciative if appropriate professionals in the Executive branch and Federal Reserve would review the attached letters I have written to the Chairman of the American Bankers Association regarding the subject. They review the history and aspects of legislative intent of the statute, the remarkable effect to date of passage (almost a 75 percent reduction among college-age students of Internet gambling in one year), the misunderstood meaning of proposed statutory changes and regulatory approaches, and the potential consequences of overturning or neutering the statute.

Sincerely,

James A. Leach

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FAX (617) 495-8957

July 24, 2008

Mr. Bradley E. Rock
Chairman
American Bankers Association
1120 Connecticut Avenue, N.W.
Washington, D.C. 20036

Dear Mr. Rock:

I appreciate your response to my letter to the Board on the subject of Internet gambling.

I recognize the banking industry's frustration with regulation. I may, also out of frustration, have exaggerated in my previous letter an assessment that the ABA has taken an "implicit position in favor of advancing a gambling culture in the United States." Nonetheless, it is unequivocally accurate to note that the ABA has gone on record and actively lobbied in support of attempts by British and American gambling interests to eviscerate what may be the only law ever to reverse the incidence of gambling in America.

In making the above assertion I am obligated to set forth precisely how in my view ABA efforts, while driven by understandable regulatory frustrations, are misdirected and counter-productive to the vested interests of America's community bankers, and why the ABA might want to reconsider whether it wishes to continue to place its reputation on the line in support of a measure in the Financial Services Committee designed principally to advance gambling interests.

1) Contention: In April the ABA testified that the statute (the Unlawful Internet Gambling Enforcement Act: UIGEA) is "unlikely to result in stopping illegal Internet gambling."

   Perspective: According to an Annenberg Public Policy Center poll, with passage of UIGEA, Internet gambling, even without implementing rules, declined from 5.8 to 1.5 percent among college-age youth (from 8.9 to 2.9 percent among males) from 2006 to 2007. And, significantly, males who reported some type of gambling on a weekly basis and who acknowledged at least one symptom of problem gambling declined from 20.4 to 5.9 percent.

For a billion people of the world the most effective anti-gambling law in history is a religious sanction, stemming from the Koran. But if the above statistics hold up (almost a 75% decline in college-age Internet gambling in one year), there could be few, if any, secular pro-savings, anti-gambling statutes to match UIGEA.

2) Contention: "ABA believes that the flaws in the definition of 'unlawful Internet Gambling' are fatal to this proposal as a legal, policy, and practical matter...A unified, practically workable definition of 'unlawful Internet gambling' must be included in either the statute or in the implementing regulations." (April ABA Testimony) "Our efforts are going to be directed to maximizing the ability of banks to rely on a common definition or categorization of illegal gambling that is of practical use and that will keep the regulatory costs in some check." (Rock July 18, 2008 letter)

Perspective: There are two principal federal statutes that relate to Internet gambling. One, the Professional and Amateur Sports Protection Act, bans Internet sports wagering other than horse racing which is covered by another statute. The other, the Wire Act, bans most other forms of gambling and games of chance.

The Justice Department over Democratic and Republican Administrations has held that the Wire Act, despite being passed in a wired telephonic era (the Kennedy Presidency), covers by extension the Internet. Gambling interests contest this proposition and argue as well that many card games like poker are games of skill rather than chance and should not be covered by the Act.

In arguing for what might seem to be a common-sense call for clarity of definition, the ABA in effect has chosen to side with gambling interests in their effort to develop loop-holes in gambling sanctions.

The goal of those lobbying for Internet gambling is through definitional exclusions to diminish the sweep of statutes like the Wire Act. But in an era of evolving technologies and rapidly changing, easily modified games of chance, loop-holes with confiscatory savings implications will inevitably spring up unless the Executive branch is allowed to maintain flexible discretion. It is definitional clarity which becomes the muddied and muddying proposition if law enforcement is straight-jacketed with methodologies to only hold accountable certain now-or-once-known games played with certain now-or-once-known technologies.

For banks, an aping of this pro-gambling position is double-unwittingness: it opens up gambling through definitional nuance and it increases confusion and hence expense in bank compliance because of the prospect that one form of card games might be within a definition and another outside, etc. Flexible, blanket restrictions are decidedly more preclusive and easier for a bank to comply with, especially, but not exclusively, if the methodology mentioned below is adopted.

While the ABA and British and American gambling interests have, in effect, been working hand-in-glove this past year in the Financial Services Committee, one would think banking and gambling interests would be incompatible. The question arises: is this a rare case of coincidence of interest or is one side snookering the other?

It is clear that gambling interests have a powerful vested interest in seeking a precise definition for "unlawful Internet gambling" – one which applies to particular games and particular processes but which implicitly then doesn't cover anything outside the framework of a precise definition, thus allowing an opening to build a vibrant gambling environment.

In contrast, it would logically seem that banking interests would want sweeping federal flexibility in defining illegal gambling coupled with governmental guidance in designating sites to be blocked from the payment system. While financial institutions should be given discretion to block gambling related transactions beyond governmental guidance, it is site clarity, rather than definitional precision, that bankers should seek. Why?

The assumption of those of us who developed and passed UIGEA was that the Executive branch would take responsibility for listing gambling sites which violate U.S. anti-gambling laws. The obligation of financial institutions was expected principally to be that of blocking payments to sites designated by the government. Such an approach simplifies compliance and takes definitional determinations off the table for most financial institutions.

3) Contention: "Some payment system operators and many banks have stated that they do not process any gambling transactions at all. ABA believes the 'safe harbor' provision should be strengthened by recognizing the right of financial institutions to block all gambling related transactions for their own reasons or discretion." (April ABA testimony)

Perspective: I find this ABA suggestion compelling, but please understand that it may underscore the desire of more than a few institutions, credit card companies in particular, to block gambling transactions to protect customers and presumably institutions themselves because of greater likelihood their customers will not default on financial system obligations. The argument for "discretion" here, while understandable and convincing to me, is inconsistent with the prior ABA argument for definitional clarity. Could it be that just as the Committee on Banking and Financial Services found it legislatively helpful simply to let the law speak for itself without adding definitional structures to UIGEA, the same reasoning might be procedurally helpful to financial institutions?

What makes UIGEA such a formidable law is that it doesn't enter the definitional thicket. It simply serves as an added – in this case, the only known effective --

enforcement mechanism for existing law which gambling interests want to weaken by limiting its reach.

As for bank liabilities, the ABA carefully and successfully pressed the Banking and Financial Services Committee to adopt a series of amendments during the seven years of consideration of UIGEA to limit bank responsibility for accidental and incidental non-compliance.

Here let me stress the self-evident: the massive intrusion of illegal Internet gambling in America has been by off-shore entities. American gaming companies operating in America have by and large been careful not to violate Internet gambling laws because they have so much at stake and are so vulnerable to prosecution. While all laws must be administered equitably, the implementation of Internet gambling laws is today principally an off-shore challenge both because that is where illegal betting volume is most extensive and the potential of money laundering most dangerous.

This off-shore Internet gambling industry which had with such impunity breached our laws is huge in magnitude but ironically doesn't precipitate many of the legally complex concerns about a citizen in one American state potentially violating a statute in another, an issue of concern set forth in the legal briefs the banking industry has developed. The internal legal complexities involving varying American state jurisdictions could become a sticky problem in the future but the emphasis today should be to follow the money, and the off-shore sites that engage in the preponderance of illegal betting generally involve blatant rather than subtle violations of U.S. statutes.

My disappointment is that the Executive branch has yet to step forward to accept legislatively mandated responsibility for rules implementation and my concern is that it may be reluctant to provide the site designation assistance needed by the banking industry. It would seem that the earlier and the firmer government acts, the less difficult enforcement is likely to be later, and the more responsibility it assumes for site designation, the less social cost and industrial burden.

4) Contention: "One very troubling trend is to increasingly try to use the banking industry for law enforcement purposes. For example, tax legislation working its way through Congress would require banks to report the credit card receipts of small businesses. As you also know, the AML/BSA costs for banks are dramatic. Every new burden is advertised as only a 'small' burden, but the cumulative effect is very large and growing." (Rock July 18, 2008 letter)

Perspective: I share these concerns, but please understand that not only is the tax legislation referenced not part of UIGEA, the motivation for its passage is somewhat different. Requiring banks to assist in tax enforcement is doing the government's business while costing and disadvantaging banks. Blocking fund transfers to gambling sites operating illegally, on the other hand, is assisting the

government in law enforcement and costing banks, but it is also advancing the vested interest of banks to strengthen a savings culture in society, one which facilitates economic growth, keeps interests rates manageable, and provides borrowers a better prospect of repaying debt.

After all, if trends toward Internet gambling were to continue at the accelerating pace witnessed from the late 1990's through 2006, a negligible savings society could rapidly tilt to a negative savings one. The current efforts of Congress and the Executive to stabilize large financial institutions from Bear Stearns to Fannie Mae and Freddie Mac will be marginal in significance if Americans come to commit disposable dollars to games of chance where the odds are always against the public, instead of saving for retirement or emergencies, a down payment on a home or mortgage obligation, or spending on goods more likely to cause general economic growth.

Internet gambling is a predatory attack on savings, and savings are the fuel of economic growth.

Einstein is said to have observed that the only real miracle was compound interest. Unfortunately, the seeds of social implosion can also be compounded. Even small "macro" reductions in savings can precipitate "micro" traumas for individual families and particular industries. If, for instance, in a given year a relatively small percentage of the public loses everything to a gambling habit and 2 or 3 percent of homeowners go belly up as a result, the costs in social cohesion as well as in our complex mortgage system could quickly become a multiple of these seemingly small numbers. Massive social instability generally involves growing minorities rather than masses of individuals in difficulty.

Put another way, we are yearly importing billions of dollars worth of Middle Eastern oil and paying for it by borrowing from Asian savings pools. With Internet gambling we are adding further to the national debt by exporting potential American savings instead of goods and services, with the recipients of these assets being a singularly unsavory class of law breakers around the globe, including ex-patriot Americans living in tax and extradition havens who face the prospect of arrest if they return.

In conclusion, the ABA is strongly on record today backing gambling industry efforts to upend a particularly unique statute. The issue can not be regarded as simply a reflection of banker angst against any new regulation. Fundamentally at issue is whether the ABA wants to continue to support a bill currently before the Congress the principal purpose of which is to unleash Internet gambling across America.

The secondary issue for the ABA is to assess what regulatory approaches are most reasonable and how most effectively to be heard by and work with regulators.

At the risk of presumption, my advice is to reverse gears in Congress, support the underlying

law rather than attempts to undercut it, re-think but upgrade input into the rule-making process, and, above all, reassess the lure and implications of Internet gambling and what its spread will mean for American society and the banking industry.

It is not lightly that I suggested in my earlier letter to the board that attention to gambling as a competitive financial industry as well as social challenge is warranted.

It is also not lightly that I affirm that the banking industry can expect significant efforts to expand gambling in America on a state-by-state as well as national Internet basis in the near future -- including a likely new charge in this Congress and certainly the next.

The gambling industry plays a strong hand in certain states and at critical junctures has involved itself within Administrations and in national elections. Now, new well-connected off-shore lobbyists are turning up in Washington and political techniques are being refined to use the Internet to advance its political agenda.

In this context, is it too much to ask financial institutions to refuse to grease Internet gambling's self-serving destructive cycle of narcissistic greed?

Is it too much to ask the Executive branch to comply with its Constitutional duty and implement regulations mandated by statute which would presumably require some public officials somewhere to track off-shore Internet criminals who assault our laws?

And is it too much to suggest to Congress in the wake of the multi-billion dollar bail-out of aspects of the housing industry, for which its lax oversight and pandering to GSEs contributed, to not saddle American taxpayers with another social expense?

When large associations take stands, the issues become one of pride as well as judgment. All I can say is that unless the ABA reconsiders its approach to a rather obscure statute, there is a very high probability that Internet gambling will become an integral part of the 21st Century American way of life. It is only because of the happenstance of a particularly unseemly scandal involving a character named Jack Abramoff that UIGEA passed in the last Congress. If this statute is overturned or eviscerated (with seemingly small tweaks in the law being potentially significant), gambling growth could become so rapid and attendant political forces so powerful that there is unlikely to be a future political remedy.

This is why I have so presumptuously approached the full board of one of the oldest and most distinguished public policy organizations in American history.

Sincerely,

James A. Leach

cc. Members of the ABA board

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JAMES A. LEACH
DIRECTOR

79 JOHN F. KENNEDY STREET
CAMBRIDGE, MASSACHUSETTS 02138
TEL (617) 495-1363
FAX (617) 495-8957

June 27, 2008

Bradley E. Rock
Chairman, President and CEO
Bank of Smithtown
Smithtown, New York

Dear Mr. Rock:

I am writing you in your role as chairman and a member of the Board of Directors of the American Bankers Association. The subject is Internet gambling and the implicit current position of the ABA in favor of advancing a gambling culture in the United States.

This week the House Financial Services Committee by a 32 to 32 vote failed to neuter a law which has a mouthful of a name – the Unlawful Internet Gambling Enforcement Act (UIGEA). The ABA stood with Las Vegas and London gambling interests in an attempt to render the statute impotent. As the author of the statute in the last Congress I would like to explain its background and implications and to suggest the ABA might want to establish a task force to study gambling with the understanding that it not only has individual family and macro-economic consequences but as the fastest growing financial industry in the world it is one of the banking industry's most virulent competitors for dollars that might otherwise become part of a savings pool or used in the economy to spur economic growth.

First, background. As a former Chairman of the House Banking and Financial Services Committee, I first introduced the approach contained in UIGEA in the late 1990s. For seven years gambling interests, largely behind the scenes, blocked passage in either the House or Senate. In the last Congress the measure was passed under regular order involving two principal committees of jurisdiction – Financial Services and Judiciary – in the House and then minutes before adjournment for the 2006 election, led by Senators Kyl and Frist, UIGEA was accepted by the Senate in an omnibus legislative package. Passage occurred in large measure because the political stars became aligned in the wake of a scandal involving a political and gambling insider named Jack Abramoff.

Over the years banking interests got and received sympathetic review – i.e., amendments – to insure that innocent financial intermediaries who are posited with modest new regulatory accountability are not unfairly penalized. Yet the issue of regulation quite naturally does not sit well with an already over-regulated industry – banking -- although interestingly after stark initial opposition, credit card companies became far more sympathetic over the years and indeed, I was told, to more than a small degree several appreciated not only the constraints contained in the bill but the legal mandate to do what they had started to try to effectuate to some degree on their own. They had discovered a vested interest in their customers' capacity to repay debt.

As for the American family and society, the three largest proponents of the legislation were the American religious community, the sports leagues (led by the NFL), and the attorneys general of the vast majority of states. Why? The one thing rabbis, imans, ministers and pastors have in common (this issue being the only one that has brought all elements of the religious community – mainline and fundamentalist churches, synagogues and mosques – together) is the professional obligation to attend to families in difficult circumstances. Every religious leader had anecdotes: thousands of anecdotes about individuals facing bankruptcy, families ruptured, even suicide attempted.

According to a group called Gamblers Anonymous (GA), the functional equivalent of Alcoholics Anonymous (AA), 2 to 4% of all who start to gamble become problem gamblers, developing a virtual addiction to the lure of making a fast buck, and most in this category lose their families, homes and jobs. Others simply dissipate disposable income.

One of the most poignant anecdotes brought to the attention of the Congress involved a minister's son who became class president at Lehigh. He got over his head gambling on the Internet, stole from his grandmother, and in a fit of guilt attempted to rob a bank to pay her back. He got caught and now as a felon his life is uniquely challenged. Another anecdote involves doing a C-Span appearance the day the House considered the vote and taking my 22 year old son, a doubter of my position, with me. All the callers that day were libertarian advocates of online gambling. Afterwards, my son told me: "See, Dad, I told you so." But then walking over to my office we bumped into a colleague from Newark in the basement of the Rayburn building who stopped and asked if my bill was coming up that day. I indicated it was and enquired where he stood on the legislation. Don looked at me and asserted that he was a big supporter. I asked him why and he responded that he knew four children of friends who had wracked up $15,000 to $25,000 in Internet gambling debts using credit cards. They were 16 years old. How, he asked, can they afford to go to college?

There is no banker anywhere who hasn't heard similar stories.

The sports leagues were adamant supporters of UIGEA because each is sensitive about the integrity of games which can so easily be influenced by a player or family member, coach or referee who might bet on their own or become associated with professional gamblers.

As for the state attorneys general, it is not generally recognized that 48 states have statutes against internet gambling, as does the U.S. government implicitly in the Wire Act and explicitly in a sports betting statute. The trouble is that enforcement has been virtually non-existent. Off-shore gambling companies have with impunity assaulted our markets and our laws. Because law which is not enforced becomes law that is not respected, UIGEA is designed to protect the rule of law and provide an enforcement mechanism for old-fashioned, common-sense, consensus statutes. It doesn't itself make Internet gambling illegal: it simply restricts banks, credit card companies and other financial intermediaries from transferring funds to Internet gambling sites, all of which operate outside of the U.S. and many of which have been closed as a result of UIGEA.

A banker might credibly ask: Why put any of the burden of enforcement on me? The answer is there is no other effective option. Two other questions must also be asked: What are the consequences of failure? And isn't it the case that the more immediately effective the effort, the less the burden is likely to be in the future?

And from the ABA's perspective the question is whether the issue should be addressed from the assumption that the glass is half full – angst about any new regulatory accountability, no matter how slight – or whether the problem is significant enough to warrant assumption of a social role and whether the legal approach on the table has not in astonishingly short order proven stunningly effective.

Perspective is often the most difficult thing to bring to issues of the day. Most American states prohibit most forms of public gambling, casino as well as Internet. The history of the states which have approved casino gambling is that credible regulation accompanies the activity. But what the Internet does is bring an unregulated casino to the work station and to the living room and kitchen of the family home. According to a national study published several years ago, problem gambling doubles within 10 miles of a gambling facility. But if an individual has access to a computer, the necessity of getting into a car and driving somewhere to enter a casino is eliminated. The computer keyboard or lap top may be less than 10 feet away.

In hearings before the Financial Services Committee several years ago a University of Illinois economist described Internet gambling as the "crack cocaine" of gambling. It is that. It is also an assault on the savings ethic. It is destructive to the general economy and particularly dispiriting to citizens who become robbed of the treasure of home ownership.

While disreputable parts of the sub-prime industry preyed on innocent home buyers, Internet gambling preys on the economy, jeopardizing the ability of families to afford the basics, including prospects of buying a home and meeting subsequent mortgage obligations. Indeed, Internet gambling can be considered an analogue to predatory lending. It is a predatory savings practice that, if allowed to take hold, could rob far more Americans of the capacity to buy and maintain a family home than all the predatory lenders combined.

The libertarian case for not restricting individual freedom of action must be respected. But in this case it is not compelling. There are simply too many social consequences that can't be ducked with Internet gambling. One relates to fairness: the regressivity of social costs; one to the damage to the American family; and one to the macro-economic consequences for society.

In response to the housing crisis, the Fed has moved to bolster financial stability from the top down through the discretion it has in influencing interest rates and providing liquidity to parts of the financial system. And the Congress has under consideration a variety of approaches to provide greater stability for stretched homeowners from the bottom up. But neither of these approaches will prove particularly consequential if our savings ethic which is under such stress by oil and food prices is further undercut by a massive increase in gambling.

Several decades ago our largest shopping mall, the Mall of Americas in Minneapolis, did a survey of who its greatest competitor for the disposable dollar was and to its surprise it found it wasn't a collection of strip malls or stores in downtown Minneapolis, but was a near-by Indian casino. Today every American merchant as well as bank competes with the technological access provided citizens to goods and services on a lap top. The question is whether the one productivity improvement brought by the Internet which is counter-productive for society is Internet gambling.

While there are no precise statistics available and no proper way for a lender to gather certain kinds of intrusive information, Iowa community bankers tell me that their sense is that 20% of all bankruptcies they work with have a gambling dimension. In my state the principal problem is river boat and Indian casino gambling but on campus and increasingly with the adult population Internet gambling started to gather momentum in the first years of this new century.

Nation-wide, from the late 1990s to 2006 the incidence of college internet gambling increased from approximately 1 to almost 6% and was expected to rise to the 10% level this year, with a doubling within another five years. But with passage of UIGEA it relapsed to 1990s levels. According to an Annenberg Public Policy Center poll, Internet gambling declined from 5.8% to1.5 % among college-age youth (from 8.9 % to 2.9% among males) from 2006 to 2007. And, significantly, males who reported some type of gambling on a weekly basis and who acknowledged at least one symptom of problem gambling dropped from 20.4% in 2006 to 5.9% in 2007.

Yet, with all the poker shows and sports betting gurus on television it is hard to visualize the wraps being kept on gambling without private sector and governmental vigilance – i.e., enforcement of law. And, frankly, it is hard to understand why the ABA is objecting to rather than celebrating the initial success of what could be considered one of the few prudent, fiscally restrained statutes of the 21s century – there being, after all, federal budget as well as commercial consequences of a gambling culture.

Just how much does it matter? Despite our great wealth, we as a country have one of the lowest savings rates in the world. It is not at all inconceivable that a movement toward Internet gambling will tilt our negligible savings into a negative savings rate. How can this be good for the American family? For the American economy? For American national security?

How can we justify playing Russian roulette with America's future?

In writing to suggest that the ABA might establish a task force on gambling as you have with other competitive industries I would be hopeful you might review not only your stance on UIGEA but think through whether all the financial literacy programs banks are associated with might not include a significant gambling education component and whether the ABA might not want to play an upgraded, activist role in politics at the state level where states like Massachusetts have under consideration initiating casino gambling and Maryland expanding slots. For politicians gambling seems to be a way to garner more revenue without raising taxes. What is never taken into consideration is that revenue that goes to gambling is revenue that doesn't go into buying food or shoes subject to sales and income taxes or wend its way through the savings system.

But please understand that your current allies in the effort this week to upend UIGEA in the House Financial Services Committee – the gambling industry – understand full well that Internet gambling could with a capricious change of law quickly surpass casino gambling in the United States. And their efforts will neither cease this year nor in subsequent Congresses.

Sincerely,

James A. Leach