



December 12, 2007

Submitted Electronically

Attn: Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th St and Constitution Ave. NW
Washington, DC 20551
Docket Number R-1298

Department of the Treasury
Office of Critical Infrastructure Protection and Compliance Policy
Room 1327, Main Treasury Building
1500 Pennsylvania Ave. NW
Washington, DC 20220
Treas-DO-2007-0015

Re: Prohibition on Funding of Unlawful Internet Gambling

Dear Board of Governors and Department of the Treasury:

The National Football League (NFL), Major League Baseball (MLB), National Basketball Association (NBA), National Hockey League (NHL), and National Collegiate Athletic Association (NCAA), appreciate the opportunity to comment on the Notice of Joint Proposed Rulemaking published in the Federal Register on October 4, 2007, at 72 Fed. Reg. 56680, et seq. ("NPRM") concerning the implementation of the Unlawful Internet Gambling Enforcement Act of 2006 ("UIGEA"). As representatives of major athletic associations that actively supported the enactment of UIGEA, we wish to see the intent of this law fully and effectively implemented through the final regulations.

Sports gambling threatens both the actual integrity of athletic contests and the perception of the fairness of such contests. It places athletes, coaches and other team personnel, as well as officials, at risk of pressure and threats from gamblers and organized crime to affect the outcome of a game or reveal confidential information. It lures young people into acceptance of a gambling lifestyle and undermines the family-friendly character of athletic events. For these reasons, the Professional and Amateur Sports Protection Act of 1992 put a stop to the proliferation of sports gambling under state laws. Soon thereafter, however, sports gambling spread on the Internet, and offshore sportsbooks fostered a widely mistaken belief among Americans that sports gambling is a legal and acceptable form of entertainment.

Though Internet gambling on athletic contests has always been unambiguously illegal under the Wire Act and numerous other federal and state laws, it is often impossible to prosecute the gambling businesses when they are located offshore in jurisdictions that deliberately harbor these operators. Moreover, it has been the consistent position of the United States to focus prosecution of illegal gambling on the operator rather than the individual gambling customer. Faced with these limitations, the Congressionally-created National Gambling Impact Study Commission recommended in 1999 that the most effective means to combat illegal online gambling would be to stop the financial transactions that fuel this black market. Between 1999 and 2006 the particulars of this concept were repeatedly refined, in consultation with financial institutions and the Congressional committees with jurisdiction over financial services, ultimately resulting in the enactment of UIGEA.

The implementing regulations for UIGEA are intended by Congress to perform an essential role in the enforcement of U.S. gambling laws. We believe the NPRM represents a solid foundation upon which effective final regulations can be built, and we appreciate the efforts of your Agencies to adhere strictly to the Congressional intent underlying UIGEA.

We particularly wish to commend the Agencies for not granting system-wide exemptions to any major payment system. The business model of the Internet gambling companies has always been to exploit any loophole in law enforcement to thwart the letter and spirit of American laws. It accordingly is entirely predictable that if any payment system were to be exempted from these regulations, Internet gambling companies would be swift to advise potential customers in the United States how they could send funds through that exempted system as a means of evading the UIGEA.

We further commend the Agencies for consciously addressing the difficulty that arises from the fact that banks serving Internet gambling operators — like the gambling operations themselves — are almost always located offshore, often outside the direct regulatory jurisdiction of the Agencies. The NPRM aims to regulate these banks indirectly, by requiring that the contractual and other business relationships between U.S. institutions and these foreign banks not be used to facilitate activity that is illegal in the U.S. In payment systems where certain participants are exempted and covered participants would often be offshore, it is necessary to regulate the U.S. participant controlling the cross-border transaction to prevent widespread evasion.

It is essential that, for each payment system, there be at least one effective “chokepoint” for restricted transactions, and that the selection of such “chokepoints” take into account the fact that the gambling operators on the receiving end of these transactions typically are banking outside of the U.S. We do not seek regulations that are more burdensome to payment system participants than are necessary, but in crafting minimally-burdensome regulations this is the one principle that is absolutely indispensable.

In furtherance of these principles, we offer the following recommendations through which the Agencies can build a stronger defense against illegal Internet gambling transactions upon the foundation that has been laid in the NPRM:

I. Shift the burden of distinguishing illegal from legal transactions to the gambling business.

Numerous other commentators have noted that, because the definition of “restricted transaction” relies on the interpretation of underlying federal and state laws and the location of the gambler at the time the gambling transaction is initiated, it would be difficult if not impossible for payment system participants to determine whether any given financial transaction is a restricted transaction, even if one party is known to engage in the Internet gambling business. Some of these commenters have raised concerns that this will cause payment system participants to “overblock” any transaction with ties to Internet gambling, even if that particular transaction happens to be legal. We disagree with any suggestion that the possibility of overblocking would justify an exemption from the regulation.

However, we believe the Agencies can illuminate a path for businesses that legitimately wish to avoid overblocking without creating undue burdens for payment system participants. Commercial customers engaged in online gambling business should be explicitly required to demonstrate to their payment service providers that they have taken adequate steps to ensure that they are not accepting bets or wagers from customers in jurisdictions where such bets or wagers are unlawful. In each jurisdiction from which a gambling business accepts bets or wagers, the gambling business should at least be able to cite the law or regulation that authorizes its online gambling activity. Because the conduct of an unauthorized commercial gambling operation is illegal in every state of the Union, a gambling operation that cannot cite its source of authorization can and should be presumed illicit. Conversely, it would be reasonable for a payment service provider to presume that a gambling business that presents authenticated documentation of authorization in each relevant jurisdiction is not engaged in restricted transactions. Even systems that rely on “coding” could avoid overblocking by using a different code for “authenticated” gambling businesses.

Moreover, we recognize that businesses engaged in gambling may also accept payment for other, non-restricted purposes. For instance, an online gambling site may also sell t-shirts and books. To distinguish these types of transactions, it is reasonable to expect the business to set up a separate account for non-gambling transactions, which could be coded differently (in the case of card systems) and allowed to accept funds without requiring authentication of gambling authorization or geographic limits. Again, by encouraging or requiring the gambling business to set up a separate account for non-gambling purposes, the burden of distinguishing legal and illegal transactions is shifted away from the payment system and onto the gambling business, where it rightly belongs.

II. Strengthen guidance for cross-border contractual requirements.

The NPRM instructs a receiving gateway operator that receives ACH debit instructions from a foreign sender to have a term in its agreement with the foreign sender that requires “the foreign sender to have reasonably designed policies and procedures in place to ensure that the relationship will not be used to process restricted transactions.” Section 6(b)(2)(i). A similar instruction applies to a depository bank that receives a check for collection directly from a foreign bank. Section 6(d)(2)(i). The final regulation should be more explicit as

to the precise nature of “reasonably designed policies and procedures” required by cross-border contracts.

Specifically, we believe that “reasonably designed policies and procedures” for a foreign sender ought to be defined as policies and procedures that are substantially similar to the safe harbor requirements for corresponding U.S. payment system participants, as defined in sections 6(b)(1) and 6(d)(1). It would also be advisable to include in the final regulation sample contractual language that would fulfill this safe harbor requirement. This would minimize legal uncertainty, regulatory burden and cost for payment system participants who are expected to include such a term in their contracts.

We also question why a similar contractual requirement is not part of the safe harbor rules for originating gateway operators that receive ACH credit transactions or banks that send wire transfers directly to foreign banks. It seems that, at least in any case where a cross-border contractual relationship already exists, a similar contractual requirement would facilitate effective enforcement at minimal burden to the payment system participant (particularly if sample language is provided by regulation).

III. Strengthen guidance for imposition of penalties.

The NPRM instructs payment system participants to have policies and procedures addressing when fines should be imposed, services denied, or relationships terminated as a penalty against other parties who transmit restricted transactions. There is no guidance as to whether it would be appropriate to impose penalties after one violation or one hundred violations, or how harsh those penalties should be. More detailed guidance would offer the regulated entities greater certainty and provide more uniform enforcement. We are particularly concerned that payment system participants may impose only nominal penalties while claiming compliance with the regulations. At the very least, the final regulation should require that penalties be reasonably designed to deter effectively the transmission of restricted transactions.

IV. Establish a list of known bad actors to facilitate enforcement.

Though the NPRM instructs payment system participants to impose penalties when restricted transactions are discovered, it gives no indication as to *how* restricted transactions might be discovered in ACH, check and wire transfer systems once customers get past the “screening” requirements. Presumably, state and federal law enforcement will be the primary source for detecting restricted transactions that are not prevented by the due diligence process. As the NPRM is presently structured, it appears that, after law enforcement determines that a restricted transaction has taken place and identifies the source of that illegal transaction, only the financial entities that were non-exempted participants in that particular transaction are required to take any action based upon this information. Such catch-as-catch-can enforcement seriously weakens the deterrent effect of the proposed regulations.

We agree with the NPRM that a list of unlawful Internet gambling businesses compiled by the Agencies would not be, by itself, an effective method for implementing UIGEA. However, we note that some payment system participants have explicitly asked for a list that would help them identify restricted transactions. While it is true that the Agencies do not

enforce or interpret gambling laws, state and federal law enforcement officials do perform this function, and the Agencies are charged with enforcing the final regulations under UIGEA. The Agencies can bring these differing enforcement functions into harmony by establishing a mechanism — in particular, an information database accessible to the regulated entities — by which law enforcement officials with authority to enforce gambling laws can efficiently inform *all* regulated payment system participants of the identity of gambling law violators, including payment system participants who fail to take appropriate steps to avoid abetting this criminal activity.

On a related note, it is not clear to us that a payment system participant who is exempted under section 4 would ever be required to block a restricted transaction, even in cases where the participant has *actual knowledge* that it is a restricted transaction. While we understand exempting participants from due diligence and monitoring requirements when they occupy certain positions in the transaction chain that would normally not be able to detect the illegal nature of the transaction, it is possible that such participants may nevertheless in some cases acquire knowledge that the transaction is restricted. For instance, the gambling business's bank may be an affiliate or law enforcement may provide the information (directly or by means of an information sharing list). The final regulations should be revised to clarify that U.S. payment system participants are not exempt from blocking a transaction, regardless of their "place in the chain," if they have actual knowledge that the transaction is a restricted transaction.

V. Consider how to cover non-traditional payment systems.

There are reports that some online casinos use 900 telephone numbers outside of the U.S. to fund accounts for U.S. customers. Under this scheme, the gambler calls a 900 number outside of the U.S., which appears as a charge on the gambler's telephone bill. The foreign business that sets up the 900 number receives payment through the phone company, and then forwards the funds to the bank of the gambling business to fund the gambler's account. In this case, it appears that no participant in a "designated payment system" (as defined in the NPRM) is domestic, so the regulations would not seem to cover this scheme.

We are not aware of the exact mechanics of the "900 number" payment system, but we urge the Agencies to investigate these reports and make sure this scheme is covered in the final regulations. Further, if other uncovered payment systems are brought to the attention of the Agencies, we strongly support your efforts to close these loopholes.

VI. Finalize promptly and reevaluate frequently.

The NPRM asks for comment on whether the final regulations should take effect six months after the joint final rules are published. We note that the implementing regulations for UIGEA are already long overdue according to the statutory mandate. Moreover, because the NPRM focuses on due diligence procedures instead of new blocking technology, we do not see any reason why payment system participants would be unable to implement final regulations promptly. Therefore, though we do not suggest a shorter period, we believe that the Agencies should issue final regulations promptly and make them effective no later than six months after such final rules are published.

If the Agencies are inclined to delay final regulations due to uncertainty about their effect, we urge you to proceed promptly and let the marketplace tell you whether changes are needed. The marketplace will provide a more objective perspective on the efficacy and appropriateness of the regulations than any one or collection of commentators. The proposed regulations are not exclusive, allowing payment system participants to develop alternative enforcement procedures in case the regulatory safe harbors prove unworkable. Moreover, as technology develops, new enforcement systems — and new evasion schemes — are likely to develop. We suggest that the regulation itself provide for frequent periodic review and revision by the Agencies to accommodate new developments in the payment services sector.

We once again thank you for your sincere efforts to write regulations that effectively implement UIGEA. We will continue to offer our cooperation and assistance to the Agencies, as well as to local, state, federal and international law enforcement, to see that gambling laws, particularly with respect to athletic competitions, are effectively enforced.

Sincerely,

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