



Department of Justice

STATEMENT

OF

**JOHN G. MALCOLM
DEPUTY ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION**

BEFORE THE

**COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE**

CONCERNING

GAMBLING ON THE INTERNET

PRESENTED ON

MARCH 18, 2003

**STATEMENT OF
JOHN G. MALCOLM
DEPUTY ASSISTANT ATTORNEY GENERAL**

**CRIMINAL DIVISION
UNITED STATES DEPARTMENT OF JUSTICE**

**BEFORE THE
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE**

Tuesday, March 18, 2003

Mr. Chairman and Members of the Committee:

Thank you for inviting me to testify before you today. The issue before this Committee is one of singular importance, and I commend the Committee for holding a hearing on this issue. I would also like to commend Senator Kyl, as well as Congressmen Goodlatte and Leach, for their tireless efforts and longstanding commitment to provide law enforcement with additional tools to combat Internet gambling. Today I am pleased to offer the views of the Department of Justice about Internet gambling, including the potential for gambling by minors and compulsive gambling, the potential for fraud and money laundering, the potential for the organized crime, and recent state actions. The Department of Justice generally supports the efforts of the drafters of these bills to enable law enforcement to cut off the transfer of funds to and from illegal Internet gambling businesses.

As you all know, the number of Internet gambling sites has increased substantially in recent years. While there were approximately 700 Internet gambling sites in 1999, it is estimated that by the end of 2003, there will be approximately 1,800 such sites generating around \$4.2 billion. In addition

to on-line casino-style gambling sites, there are also numerous off-shore sports books operating telephone betting services. These developments are of great concern to the United States Department of Justice, particularly because many of these operations are currently accepting bets from United States citizens, when we believe that it is illegal to do so.

The Internet and other emerging technologies, such as interactive television, have made possible types of gambling that were not feasible a few years ago. For example, a United States citizen can now, from his home at any hour of the day or night, participate in an interactive Internet poker game operated by a computer located in the Caribbean. Indeed, a tech-savvy gambler can route his bets through computers located in other countries throughout the world, thereby obscuring the fact that he is placing his bet from the United States or from some other country where it is illegal to do so.

Gambling by Minors

On-line gambling also makes it far more difficult to prevent minors from gambling. Gambling websites cannot look at their customers to assess their age and request photo identification as is possible in traditional physical casinos and Off-Track-Betting parlors. Currently, Internet gambling businesses have no reliable way of confirming that the gamblers are not minors who have gained access to a credit card and are gambling on their web site. Although some companies are developing software to try to detect whether a player is old enough to gamble or whether that player is from a legal jurisdiction, such software has not been perfected and would, of course, be subject to the same types of flaws and vulnerabilities that could be exploited by hackers.

Compulsive Gambling

Unlike on-site gambling, on-line gambling is readily available to all at all hours and it permits the user to gamble, in many cases, anonymously. This presents a greater danger for compulsive gambling and can cause severe financial consequences for an unsuccessful player. As was recently pointed out by the American Psychiatric Society: "Internet gambling, unlike many other forms of gambling activity, is a solitary activity, which makes it even more dangerous; people can gamble uninterrupted and undetected for unlimited periods of time." Indeed, the problems associated with pathological and problem gamblers, a frighteningly-large percentage of which are young people, are well-established and can be measured in the ruined lives of both the gamblers themselves and their families.

Potential for Fraud

Although there are certainly legitimate companies that are either operating or want to operate on-line casinos in an honest manner, the potential for fraud connected with casinos and bookmaking operations in the virtual world is far greater than in the physical realm. Start-up costs are relatively low and cheap servers and unsophisticated software are readily-available. On-line casinos and bookmaking establishments operate in many countries where effective regulation and law enforcement is minimal or non-existent. Like scam telemarketing operations, on-line gambling establishments appear and disappear with regularity, collecting from losers and not paying winners, and with little fear of being apprehended and prosecuted.

Through slight alterations of the software, unscrupulous gambling operations can manipulate the odds in their favor, make unauthorized credit card charges to the accounts of unsuspecting gamblers, or alter their own accounts to skim money. There is also a danger that

hackers can manipulate the online games in their favor or can steal credit card or other information about other gamblers using the site.

Potential for Organized Crime

Additionally, the Department of Justice has a concern about the potential for the involvement of organized crime in Internet gambling. Traditionally, gambling has been one of the staple activities in which organized crime has been involved. Indeed, many of the recent indictments brought against members of organized crime groups have included gambling charges. We have now seen evidence that organized crime is moving into Internet gambling.

Internet Gambling Violates Federal law

Most of these gambling businesses are operating offshore in foreign jurisdictions. If these businesses are accepting bets or wagers from customers located in the United States, then these businesses are violating federal laws, including Sections 1084, 1952, and 1955 of Title 18, United States Code. While the United States can bring indictments against these companies or the individuals operating these companies, the federal government may not be able to bring such individuals or companies to trial in the United States.

Money Laundering and Internet Gambling

Another major concern that the Department of Justice has about on-line gambling is that Internet gambling businesses provide criminals with an easy and excellent vehicle for money laundering, due in large part to the volume, speed, and international reach of Internet transactions and the offshore locations of most Internet gambling sites, as well as the fact that the industry itself is already cash-intensive.

It is a fact that money launderers have to go to financial institutions either to conceal

their illegal funds or recycle those funds back into the economy for their use. Because criminals are aware that banks have been subjected to greater scrutiny and regulation, they have -- not surprisingly -- turned to other non-bank financial institutions, such as casinos, to launder their money. On-line casinos are a particularly inviting target because, in addition to using the gambling that casinos offer as a way to hide or transfer money, casinos offer a broad array of financial services to their customers, such as providing credit accounts, fund transmittal services, check cashing services, and currency exchange services.

Individuals wanting to launder ill-gotten gains through an on-line casino can do so in a variety of ways. For example, a customer could establish an account with a casino using illegally-derived proceeds, conduct a minimal amount of betting or engage in offsetting bets with an overseas confederate, and then request repayment from the casino, thereby providing a new “source” of the funds. If a gambler wants to transfer money to an inside source in the casino, who may be located in another country, he can just play until he loses the requisite amount. Similarly, if an insider wants to transfer money to the gambler, perhaps as payment for some illicit activity, he can rig the game so the bettor wins.

The anonymous nature of the Internet and the use of encryption make it difficult to trace the transactions. The gambling business may also not maintain the transaction records, in which case tracing may be impossible. While regulators in the United States can visit physical casinos, observe their operations, and examine their books and records to ensure compliance with regulations, this is far more difficult, if not impossible, with virtual casinos.

Other Recent State Actions

In addition to the federal government, various state governments have also taken actions against on-line gambling. For instance, in New York State, where unauthorized gambling is illegal, the New York State Attorney General reached an agreement with Citibank to block credit card payments of on-line gambling transactions by its customers. The same Attorney General recently reached an agreement with PayPal, which agreed to stop processing payments from New York State customers to on-line gambling merchants.

Some companies have taken steps themselves against on-line gambling businesses. For instance, in 2002 PayPal was acquired by E-Bay, the on-line auction service, which announced that it would phase out PayPal's on-line gambling. Both Discover and American Express have company policies that restrict the use of their credit cards for Internet gambling and prevent Internet gambling sites from being issued credit card merchant accounts.

Conclusion

On behalf of the Department of Justice, I want to thank you again for inviting me to testify today. We thank you for your support over the years and reaffirm our commitment to work with Congress to address the significant issue of Internet gambling. While we have some technical and other concerns about these bills, we support the sponsors' efforts to address gambling on the Internet. I will be happy to answer any questions that you might have.