

UNLAWFUL INTERNET GAMBLING ENFORCEMENT ACT (UIGEA) REGULATIONS

Public Comment Period Ends December 12, 2007

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WRITE YOUR COMMENTS:

- The Board of Governors of the Federal Reserve System and Departmental Offices (Board)
- The Department of the Treasury (Treasury).

Important Date: *Comments are due by December 12, 2007.*

[Please submit copies of comments to both Board and Treasury Departments.]

SIX CONCERNS WITH THE PROPOSED REGULATIONS:

Five areas within the UIGEA regulations should be strengthened. Consider including several of these points – or all – within your comments to the Board and Treasury.

(1) Require Foreign Institutional Contracts to Follow Existing “Know Your Customer” Regulations

The proposed regulations say U.S. financial businesses should require their foreign business partners to have "reasonable" screening procedures to stop illegal Internet gambling payments. It is hard to know what this means. The requirements for foreign business partners should be more detailed, following the model of "Know Your Customer" requirements for U.S. banks.

(2) Avoid “Overblocking” Through Creation of Separate Accounts

Some people have complained that the regulations might cause "overblocking" of legal financial transactions. The regulations should make it clear that companies who wish to do legitimate business in the U.S. can easily avoid this problem by setting up separate accounts that they certify and verify will not be used for anything that violates Federal or State gambling laws. [When a business walks the line of legal and illegal activity, it should be the responsibility of the business to make sure it stays on the right side. It should not get a free pass for walking on the illegal side of the line just because it takes some steps on the legal side.]

(3) Uncovered Forms of Payment

The regulations need to cover novel forms of payment. For instance, some Internet gambling accounts are funded by calling a 900 telephone number in Canada, and this scheme does not seem to be covered by the proposed regulations. The regulations should cover this, and should be revised frequently to cover new schemes that pop up in the future.

(4) Law Enforcement: Sharing Information

The U.S. government should set up or facilitate an information-sharing portal that would allow banks, other private entities, and state and federal law enforcement to share information about UIGEA violators. This would improve detection and enforcement.

(5) Governmental List of Unlawful Gambling Operations

The U.S. government should establish a few dedicated investigators to find and report unlawful Internet gambling transactions or operations to financial

institutions, to lessen the burden for financial institutions and improve enforcement.

(6) Parameters for Applying Penalties

The proposed regulations say U.S. financial businesses should impose penalties on business partners who fail to screen out illegal Internet gambling payments, but they don't say when penalties should be applied or how harsh they should be. The regulations should be more specific about these penalties, to make sure they effectively deter banks from aiding illegal Internet gambling.

SEND COMMENTS TO THE BOARD OF GOVERNORS:

[Board of Governors of the Federal Reserve System]

You may submit comments, identified by **Docket Number R-1298**, by any of the following methods:

- **Agency Web site:** <http://www.federalreserve.gov> .
 - Follow the instructions for submitting comments at <http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm> .
- **Federal eRulemaking Portal:** <http://www.regulations.gov> . Follow the instructions for submitting comments.
- **E-mail:** regs.comments@federalreserve.gov . Include docket number R-1298 in the subject line of the message.
- **Fax:** (202) 452-3819 or (202) 452-3102.

All public comments are available from the Board's Web site at <http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm>, as submitted, unless modified for technical reasons. Accordingly, your comments will not be edited to remove any identifying or contact information.

SEND COMMENTS TO THE TREASURY:

Federal e-Rulemaking Portal – “Regulations.gov”:

- Go to <http://www.regulations.gov>,

- Select “Department of the Treasury – All” from the agency drop-down menu,
- Then click “Submit.”
- In step four, select the “Docket ID” drop-down option, and enter “**Treas-DO-2007-0015**” and select "Exact Phrase" to submit or view public comments and to view supporting and related materials for this notice of proposed rulemaking.
- When the document links come up, click on the yellow-bubble hyper-link under the "Comments Add/Due By" header and add your comments.

The “User Tips” link at the top of the www.regulations.gov home page provides information on using Regulations.gov, including instructions for submitting or viewing public comments, viewing other supporting and related materials, and viewing the docket after the close of the comment period.
<http://www.regulations.gov/fdmspublic/component/main>

Viewing Comments Electronically All public comments are available from the Board's Web site at
<http://www.federalreserve.gov/generalinfo/foia/ProposedRegs.cfm>

CC: Board of Governors of the Federal Reserve System

FURTHER INFORMATION:

BOARD OF GOVERNORS: Christopher W. Clubb, Senior Counsel (202/452-3904), Legal Division; Jack K. Walton, II, Associate Director (202/452-2660), Jeffrey S. Yeganeh, Manager, or Joseph Baressi, Financial Services Project Leader (202/452-3959), Division of Reserve Bank Operations and Payment Systems; for users of Telecommunication Devices for the Deaf (TDD) only, contact 202/263-4869.

TREASURY: Charles Klingman, Deputy Director , Office of Critical Infrastructure Protection and Compliance Policy; Steven D. Loughton, Senior Counsel , or Amanda Wise, Attorney-Advisor, Office of the Assistant General Counsel (Banking & Finance), 202/622-9209.

SUMMARY:

Summary of Proposed Internet Gambling Regulations

Overview: No payment systems are exempted – domestic participants who can reasonably detect gambling payments are directly regulated, and offshore participants are indirectly regulated by contract.

On October 1, 2007, the Department of the Treasury and the Board of Governors of the Federal Reserve jointly issued proposed regulations as required by the Unlawful Internet Gambling Enforcement Act of 2006 (“UIGEA”). UIGEA required these agencies to designate payment systems that may be used to engage in “restricted transactions” and to prescribe regulations for these payment systems to *identify and block* or otherwise *prevent or prohibit* restricted transactions. A “restricted transaction” is the receipt of funds by a gambling business in connection with unlawful Internet gambling.

The statute required the regulations to take the form of *non-exclusive examples* that would be deemed reasonable procedures for stopping restricted transactions. A payment system following the examples would be assured of being in compliance, but payment systems developing alternative procedures might have to prove that those procedures are “reasonably designed” to stop restricted transactions. Thus, stronger private initiatives are permitted, while procedures that are weaker than the regulation examples would be legally risky for financial institutions.

The proposed regulations address two general categories of payments: payments within proprietary networks and transfers between depository institutions. The overarching approach is sensible:

- Where U.S. entities have any reasonable possibility of discovering that the recipient of funds is a gambling business breaking the law, they are required to take affirmative steps to prevent illicit use of their payment systems.
- Where the only entities who could know the nature of the financial transaction are outside of U.S. borders and thus beyond the reach of U.S. regulatory power, the regulations instruct the U.S. institutions facilitating cross-border transactions to use contractual language and private remedies to require the foreign operators to screen out customers who violate U.S. gambling law.

Payments Within Proprietary Networks

This includes credit cards and all other card systems (e.g. debit cards, stored value cards) and money transmitting systems (e.g. Western Union, PayPal). Because these payment systems operate through proprietary networks, all or most of the participants in the system can access information about where the money is coming from and where it is going to, and potentially even what the money is paying for. These systems are instructed to screen potential commercial customers, forbid customers from receiving restricted transactions, monitor use of their systems for suspicious activity, monitor

unauthorized use of their trademarks, and impose penalties on violators. Credit cards are also instructed to continue the already-common practice of using merchant business category codes to deny authorization for certain transactions.

Transfers Between Depository Institutions

This includes checks, wire transfers, and Automated Clearing House transactions (ACH, which is the way most transfers between bank accounts now take place, including electronically-processed physical checks). As these systems are structured, each transaction only carries bank routing data as it travels through a non-proprietary transfer system. The sending bank knows nothing of the receiving bank other than an account number. Short of requiring these financial systems to radically overhaul their practices, the only way to stop restricted transactions is to screen out commercial customers who receive them. Thus, banks are instructed to screen commercial customers and impose penalties for illicit use, and the U.S. entity with direct offshore contacts is also instructed to impose penalties on foreign operators who transmit restricted transactions. In certain cases, the U.S. entity with foreign contacts is also instructed to include provisions in its contracts with foreign operators requiring the foreign operator to have reasonably designed policies and procedures for preventing restricted transactions.

When depository institutions are *not* acting in these capacities, they are exempted from the regulations. Thus, for example, if a U.S. bank receives an illicit payment instruction through another U.S. entity, but the Internet gambling company has no customer relationship to that receiving bank, the bank is not required to block the transaction. The bank is exempted because it is not in a position to know that the transaction is coming from an Internet gambling business.