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REPORT TO THE TRADE BARRIERS

REGULATION COMMITTEE

(Commission Staff Working Paper)

**EXAMINATION PROCEDURE CONCERNING AN OBSTACLE TO TRADE,
WITHIN THE MEANING OF COUNCIL REGULATION (EC) No 3286/94,
CONSISTING OF MEASURES ADOPTED BY THE UNITED STATES OF
AMERICA AFFECTING TRADE IN REMOTE GAMBLING SERVICES**

COMPLAINT SUBMITTED BY THE REMOTE GAMBLING ASSOCIATION (RGA)

[...] indicates information considered confidential in the sense of Article 9 of the
Trade Barriers Regulation

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ACRONYMS

AGTOA.....	American Greyhound Track Operators Association
AHC.....	American Horse Council
DOC.....	Department of Commerce
DOJ.....	Department of Justice
DOS.....	Department of State
DOT.....	Department of the Treasury
DSU.....	Dispute Settlement Understanding
EC.....	European Communities
ECJ.....	European Court of Justice
EU.....	European Union
GAO.....	General Accounting Office
GATS.....	General Agreement on Trade in Services
GATT.....	General Agreement on Tariffs and Trade
GGR/GGY....	Gross Gaming Revenue/Gross Gaming Yield
IGBA.....	Illegal Gambling Business Act
IHA.....	Interstate Horseracing Act
IPO.....	Initial public offering
ITWA.....	Interstate Transportation of Wagering Paraphernalia Act
NASPL.....	North American Association of State and Provincial Lotteries
NTRA.....	National Thoroughbred Racing Association
PASPA.....	Professional and Amateur Sports Protection Act
RGA.....	Remote Gambling Association
RICO.....	Racketeer Influenced and Corrupt Organizations Act
UIGEA.....	Unlawful Internet Gambling Enforcement Act
US.....	United States of America

USAM..... United States Attorney's Manual
USC United States Code
USTR..... United States Trade Representative
WLA..... World Lottery Association
WTO..... World Trade Organization

EXECUTIVE SUMMARY

A. Introduction

On 20 December 2007, the Remote Gambling Association ("RGA") lodged a complaint pursuant to Article 4 of Council Regulation (EC) No 3286/94 (hereinafter the "Trade Barriers Regulation") concerning what was described as the United States' WTO-illegal ban on foreign Internet gambling providers and its allegedly discriminatory enforcement against EU companies. The complaint claimed that these US measures were inconsistent with Articles XVI (Market Access) and XVII (National Treatment) of the GATS, and were not justified under Article XIV (General Exceptions) of the GATS. The Commission, after consulting the Trade Barriers Regulation Committee, initiated an examination procedure on 11 March 2008.

The Commission services gathered information and comments from Community and US suppliers of remote gambling and betting services; Community and US suppliers of supporting services to the remote gambling and betting services industry; Community and US suppliers of lottery services; the US government; and from the EU Member States concerned. A verification visit took place in the US from 15 to 18 September 2008.

The proceeding concerns primarily the supply of gambling and betting services delivered via remote communication and primarily the Internet. This service falls under subsector 96492 "gambling and betting services", sector 964 "Sporting and other recreational services" of the "Services sectoral classification list" (the so-called "W/120 list") used in the GATS context.

B. Factual background

The EU has established a world-wide leading industry in the area of remote gambling and betting services. The size of the online market is substantial, with estimates of the total size of the world remote gambling and betting market surpassing \$14 billion in 2007, out of a total global market of gambling and betting of \$335 billion. Around \$6 billion thereof correspond to the EU online market, while the size of the US online market is estimated at \$4 billion. The total size of the EU gambling and betting market is estimated at \$116 billion, and the US market at \$110 billion. Moreover, a number of factors are likely to underpin substantial growth in the demand for remote gambling: increasing penetration of computers, the Internet and broadband connections; development of more user-friendly and increasingly integrated technologies; safer electronic financial transactions; increase in leisure spending; etc. All these factors determine the continued growth of the market in the next few years, with estimates of the size of the world market for 2010 surpassing \$22 billion.

EU companies had been active on the US market until 2006, where they generated a substantial share of their revenue.

C. The challenged measures and obstacles to trade

The complaint concerns alleged trade barriers maintained by the US consisting of legislation imposing a ban on internet gambling; the measures taken to enforce that legislation; and the fact that the legislation is enforced in a discriminatory way. The investigation has confirmed that the US applies a prohibition on the cross-border supply

of gambling and betting services into the US territory, and that in parallel certain types of remote supply of gambling and betting services are allowed within the US, both on an intrastate and interstate basis. This is notably the case with regard to remote gambling on horse racing and greyhound racing.

The investigation has addressed the question of the impact that the likely withdrawal of the US GATS commitments on gambling and betting services would have on a potential WTO case against the US, and concludes that, to the extent that US enforcement actions against EU companies are based on services trade that took place while the US GATS commitments were in place, the US would continue to be bound by its GATS commitments in respect of such past trade.

The investigation has shown that the US measures under investigation are inconsistent with the WTO agreements. Furthermore, it has concluded that the measures cannot be justified on grounds of public policy concerns given notably the fact that some types of remote supply are allowed in the US, and that alternative measures in the form of strict regulation of the supply of the service are currently being used in the US to address the relevant public policy concerns.

D. Adverse trade effects

The obstacles to trade identified in the complaint have forced the total withdrawal and/or absence of EU companies from the US market and have significant additional negative effects on their business outside the US. It is evident that the Community enterprises affected by the US measures have suffered, and continue to suffer, adverse effects as a result of the US measures under investigation. Moreover, there is a threat of additional adverse trade effects that could develop into actual adverse trade effects. These adverse trade effects have a material impact on a sector of economic activity and on a region of the Community.

The obstacles to trade can therefore be considered as causing and threatening to cause adverse trade effects, having a material impact on a sector of economic activity and a region of the Community.

E. Community interest

The EU has developed the world's leading internet gaming business. Many of the world's largest companies are licensed in and operate from the UK, Gibraltar, Malta, Ireland and Austria. There are significant back office operations providing technology, marketing and customer service support in other Member States. Although accurate statistics on this sector are not readily available, the sector is economically significant, with an estimate of more than 10,000 staff employed by the internet gaming industry in the EU. Moreover, the Internet gaming sector has a significant indirect economic impact on other sectors of the economy which are involved in providing the infrastructure that an internet business requires (primarily financial services, information technology and professional services).

Leaving possible divergent economic interests of the various actors (notably online vs. offline) in this sector aside, it has to be borne in mind that different parts of the Community industry should in principle compete with one another without the interference of WTO-inconsistent distortions. Such economic considerations relating to other actors in the sector do not outweigh the interests of the Community that favour taking action.

The Commission services are aware of the important public policy concerns involved in the area of gambling and betting services, and recall in this sense recital four of the preamble of the GATS, recognizing the right of Members to regulate, and to introduce new regulations, on the supply of services within their territories in order to meet national policy objectives. The WTO Agreement, and the GATS in particular, provide Members with the necessary flexibility to pursue the relevant policy objectives. It is however essential that WTO Members pursue their policy objectives with full respect of their international obligations

The Global Europe Communication from October 2006 calls for activism in creating open markets and fair conditions for trade abroad. In this context, it is important to ensure that other WTO Members, and in particular the US, observe international trade rules, and the obligations contained in the WTO Agreement.

It can therefore be concluded that it is in the interest of the Community to act in respect of the obstacles to trade identified in this investigation.

F. Conclusion

The investigation has revealed that US laws prohibiting the cross-border supply of remote gambling and betting services as well as their enforcement against Community companies are in violation of Articles XVI and XVII of the GATS, and are not justified under Article XIV of the GATS. As a consequence, the investigation has established the existence of an obstacle to trade in the sense of the Trade Barriers Regulation. Moreover, the investigation has shown that adverse trade effects within the meaning of the Trade Barriers Regulation exist and have been caused by the obstacles to trade identified. Finally, the investigation has concluded that action is necessary in the interests of the Community.

It should nonetheless be noted that the subsequent steps in this Trade Barriers Regulation procedure would need to take account of the state of play in the ongoing process towards the withdrawal of the US GATS commitments on gambling and betting services, especially given that the definition of the measures at issue and the remedy reasonably available to the EC under WTO rules may be affected by the withdrawal. Moreover, the approach that the new US Administration takes with regard to the subject matter under investigation in this Trade Barriers Regulation examination may also be relevant for determining which subsequent acts are in the interest of the Community.

A. INTRODUCTION

A.1. The complaint

On 20 December 2007, the Remote Gambling Association ("RGA") lodged a complaint pursuant to Article 4 of Council Regulation (EC) No 3286/94 (hereinafter the "Trade Barriers Regulation") concerning what was described as the United States' WTO-illegal ban on foreign Internet gambling providers and its enforcement. The complaint targeted in particular the enforcement of the ban against EC companies for activities conducted in the US until October 2006. The complaint alleged that the prohibition to supply gambling and betting services from abroad contained in US federal legislation, together with enforcement actions directed against foreign suppliers but not against US suppliers, amounted to violations of Articles XVI (Market Access) and XVII (National Treatment) of the General Agreement on Trade in Services (GATS) which, in addition, could not be justified under Article XIV (General Exceptions) of the GATS. The complaint further maintained that the obstacle to trade so identified had forced the total withdrawal of EU suppliers from the US market and had further significant, adverse effects both on the business of these suppliers outside the US and on the EU gaming sector more broadly, as well as on EU financial services companies. Finally, the complaint alleged that it was in the EU's interest to launch an investigation in order to ensure that WTO rules and obligations were respected, and requested the Commission to open an investigation under the Trade Barriers Regulation.

A.2. Standing of the complainant

The complainant is a London-based trade association including in its membership several of the main Community enterprises offering remote gambling and betting services.¹ It is therefore an "association, having or not legal personality, acting on behalf of one or more Community enterprises" in the sense of Articles 2.6 and 4.1 of the Trade Barriers Regulation.

Of the nine RGA members in the top ten EU service providers referred to in the complaint, Ladbrokes, William Hill, Gala Coral Group, Betfair (for sports betting) and Sportingbet are registered in the UK; Unibet and Betfair (for games, casino and poker) are registered in Malta; Paddypower is registered in Ireland; Partygaming and 888 Holdings are registered in Gibraltar which, although part of the Community, is not a Member State. Talarius and Bet 365, which are not among the top ten EU service providers listed in the complaint, are both registered in the UK.

The Commission services consider that also those RGA Members that are registered in Gibraltar have to be considered "Community enterprises" within the meaning of Article 2.6 of the Trade Barriers Regulation. This Article provides:

"The term "Community enterprise" shall be taken to mean a company or firm formed in accordance with the law of a Member State and having its registered office, central administration or principal place of business within the Community, directly concerned by the production of goods or the provision of services which are the subject of the obstacle to trade."

¹ A list of members of the RGA is attached as annex 1

The RGA Members registered in Gibraltar fulfil the third element of this definition since they are directly concerned by the provision of services (i.e. remote gambling and betting services) which suffer the relevant obstacle to trade.

They also comply with the second criterion of having their "registered office ... within the Community". Gibraltar is part of the Community. This follows from Article 299(4) EC, which provides that "[t]he provisions of this Treaty shall apply to the European territories for whose external relations a Member State is responsible". The UK is responsible for the external relations of Gibraltar.

RGA Members registered in Gibraltar also meet the first condition of being "formed in accordance with the law of a Member State". Although Gibraltar is technically speaking not "a Member State", companies formed in accordance with the law of Gibraltar qualify as "formed in accordance with the law of a Member State".

This follows, first, from a comparison with the parallel provision in Article 48 of the EC Treaty, which refers to "companies or firms formed in accordance with the law of a Member State...". Article 48 does apply to Gibraltar companies, unless otherwise established in applicable secondary legislation.²

Secondly, secondary legislation relating to the internal market, although addressed to Member States, without any express reference to Gibraltar, is also applicable to Gibraltar. Specifically, it is the UK who responsible for the application of Community law in Gibraltar. The UK can be held responsible for the failure to implement specific Directives in respect of Gibraltar.³ References to Member States in secondary legislation are therefore meant to include Gibraltar, unless otherwise specified. The same approach applies in respect of the trade in services aspects of the common commercial policy relevant in this examination: unless expressly excluded, the principle is that Gibraltar is covered in respect of those trade in services aspects. The Trade Barriers Regulation does not contain any express exclusion in respect of those services aspects.

Thirdly, service providers registered in Gibraltar would be part of "a Community industry" within the meaning of Articles 3 and 2.5 of the Trade Barriers Regulation. The definition of "Community industry" shows that the intention of the drafters of the Regulation was to cover all Community providers under the Trade Barriers Regulation. It would not make sense to follow a different approach for complaints brought under Article 4 of the Regulation.

² As indicated above, Article 299(4) EC provides that "[t]he provisions of this Treaty shall apply to the European territories for whose external relations a Member State is responsible". The UK is responsible for the external relations of Gibraltar. Therefore, unless expressly excluded, Community law applies to Gibraltar. Exclusions in primary legislation are contained in Articles 28, 29 and 30 of the Act of Accession of the UK to the EC, according to which certain Treaty provisions do not apply to Gibraltar. In summary, these exclusions refer to the common agricultural policy; acts on the harmonisation of legislation of Member States concerning turnover taxes; and the customs territory of the Community. The exclusion from the customs territory of the Community has implications both with respect to the internal market and the common commercial policy, as goods imported into Gibraltar are not subject to the customs duties of the common customs tariff, and are not covered by Treaty rules on free movement of goods.

³ See e.g. Case C-489/01 Commission of the European Communities v. United Kingdom

In conclusion, the reference to the "law of a Member State" in Article 2.6 of the Trade Barriers Regulation should be understood as covering also the law of Gibraltar, despite the fact that Gibraltar is not a Member State.⁴

A.3. The service

The service at issue is described in the complaint as the supply of commercial gambling and betting services delivered via remote communication and primarily the Internet.

The complaint further adds that the service can be subdivided in four different subcategories:

- Online and telephone bookmaking and pool or "pari mutuel" betting in which the participants bet on the outcome of sports or other events against the commercial operator (i.e. the bookmaker) or the "pool" of bettors.
- Online casino gaming in which the participant plays games of chance, such as roulette and "slots", against the commercial operator.
- Online card play (in particular poker) in which participants play card games against other individuals (as opposed to playing against the commercial operator).
- Online betting exchanges, in which participants bet on the outcome of sports or other events against other individuals on an "exchange" (as opposed to betting against the commercial operator or the "pool").

However, this classification is by no means the only possible way of subdividing remote gambling and betting services. For example, the "Study of Gambling Services in the Internal Market of the European Union"⁵, commissioned by the European Commission, offers several classifications. First, it makes a general distinction between what it terms "online and off-line market sectors", which it then subdivides into: betting services (including on horse and dog racing, event betting and pool competitions); bingo services; casino services; gambling services for organised charities and non-profit organisations; services of gambling machines; lottery services; media gambling services; and promotional games.⁶ Second, the same study classifies the sectors of the remote gambling industry in the EU as including: betting; lotteries; casino gaming (including card games such as poker); and bingo.⁷ Finally, it offers a further classification of remote

⁴ It should be noted that the issue of whether Gibraltar-based companies are "Community enterprises" is not directly relevant for the outcome of the current procedure. In any event, the impact of the US measures on Gibraltar-based enterprises would need to be considered for the purpose of the analysis of adverse trade effects given that, in light of their close interaction with the economy of Community Member States and notably the UK, their evolution is bound to have a serious impact on other Community enterprises. Both Partygaming and 888 Holdings are listed on the International Main Market of the London Stock Exchange

⁵ "Study of Gambling Services in the Internal Market of the European Union". Final Report, 14 June 2006. Swiss Institute of Comparative Law

⁶ Ibid., p. v

⁷ Ibid., p. 1406

gambling based on the "market channels" used: Internet; mobile phones/other devices; and interactive television.⁸

The "Study of Gambling Services in the Internal Market of the European Union" referred to above indicates that "[E]ven if not all Member States have a legal definition of the concepts of "Games of Chance" and "Gambling", in most European countries a game of chance is defined as a game that offers an opportunity to compete for prizes, where success depends completely or predominantly on coincidence or an unknown future event and cannot be influenced by the player. One of the players at least loses his or her stake."⁹

A recent progress report¹⁰ prepared by the EU Presidency on the basis of discussions held in the Working Party on Establishment and Services on the legal framework for gambling and betting and the policies of the Member States thereon notes that "although most of the various types of gambling exist in all member States, definitions may vary."¹¹ It also notes that "[T]he rules on access to online gambling and betting are frequently more restrictive..."¹² and that "forms of gambling and betting that are permitted in the various Member States are also mostly permitted online".¹³

A report¹⁴ to the US Congress by the US General Accounting Office (GAO) defines "Internet gambling" as including "any activity that takes place via the Internet and that includes the placing of a bet or wager".

In the absence of a definition of gambling and betting in EU legislation, the Commission services will for the purpose of this investigation use a definition based on the ordinary meaning of the terms "gambling and betting".

"Gambling" can be defined as "[T]he act of risking something of value, especially money, for a chance to win a prize".¹⁵ Also, according to the definition in The Shorter Oxford English Dictionary quoted by the Panel in US – Gambling,¹⁶ "to gamble" is to "play games of chance for (a lot of) money; indulge in betting, esp. habitually; risk money, fortune, success, etc., on the outcome of an event [...]."

⁸ Ibid., p. 1408

⁹ Ibid. p. p. vi

¹⁰ Progress Report – Gambling and betting: legal framework and policies in the Member States of the European Union. Prepared by the Presidency with a view to the Competitiveness Council on 1 and 2 December 2008

¹¹ Ibid., footnote 1

¹² Ibid., p. 3

¹³ Ibid., p. 14

¹⁴ "Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002.

¹⁵ Black's Law Dictionary. Eighth Edition

¹⁶ Panel Report, *US-Gambling*, para. 6.20

A bet can be defined as "[S]omething (especially money) staked or pledged as a wager".¹⁷ A wager in turn can be defined as "[M]oney or other consideration risked on an uncertain event".¹⁸ Also, according to the definition in The Shorter Oxford English Dictionary quoted by the Panel in US – Gambling,¹⁹ "to bet" is to "stake (an amount of money, etc.) against another's in support of an affirmation or on the outcome of a doubtful event; risk an amount of money etc. against (a person) by agreeing to forfeit it if the truth or outcome is not as specified. [...]"

The service at stake in this investigation can therefore be defined as a service allowing private individuals to play games that involve risking something of value for a chance to win a prize.

The investigation will focus in particular on gambling and betting services delivered via remote communication and primarily the Internet, given that the complainant is an association of enterprises that provide remote gambling and betting services. The distinguishing feature of remote gambling and betting is that consumers use certain technological means that allow them to gamble and bet remotely.

The service falls under subsector 96492 "gambling and betting services", sector 964 "Sporting and other recreational services" of the "Services sectoral classification list"²⁰ (the so-called "W/120 list") used in the GATS context.

A.4. Hearings

A.4.1. Hearing with the European State Lottery and Toto Association ("European Lotteries")

In accordance with the request by European Lotteries, dated 10 April 2008, a hearing pursuant to Article 8.5 of the Trade Barriers Regulation was held on 26 June 2008. At the hearing, European Lotteries addressed various issues relating to the points made in their 10 April submission. In support, they provided a document outlining the issues that they discussed at the hearing and annexed a document regarding ECJ case law on gambling. This document carries the title "Outline of the Oral Observations on behalf of the European State Lottery and Toto Association".

European Lotteries further requested a hearing together with the complainant (cf. A.4.4.).

A.4.2. Hearing with Stanleybet International

In accordance with the request by Stanleybet International, dated 10 April 2008, a hearing pursuant to Article 8.5 of the Trade Barriers Regulation was conducted on 27 June 2008. At the hearing, Stanleybet International addressed various issues relating to

¹⁷ Black's Law Dictionary. Eighth Edition

¹⁸ Black's Law Dictionary. Eighth Edition

¹⁹ Panel Report, *US-Gambling*, para. 6.21

²⁰ MTN.GNS/W/120 (10 July 1991)

the points made in their 10 April submission, and provided a written document entitled “US Trade Barrier Regulations”, summarising the business of Stanleybet International.

A.4.3. Hearing with the World Lottery Association (WLA) and the North American Association of State and Provincial Lotteries (NASPL)

In accordance with the requests by WLA and NASPL, and in accordance with their wish, dated 9 April 2008, a joint hearing with both WLA and NASPL pursuant to Article 8.5 of the Trade Barriers Regulation was held on 27 June 2008. At the hearing, WLA and NASPL developed various issues relating to the points made in their 9 April letters. A written copy of the oral statement by WLA was provided, as well as a document entitled “Written Observations Developed on behalf of the World Lottery Association and the North American Association of State and Provincial Lotteries”.

A.4.4. Hearing with RGA and European Lotteries

On 17 July 2008, the European Commission gave European Lotteries and RGA an opportunity to meet, so that opposing views and rebuttal arguments could be presented. This followed a request by European Lotteries, dated 26 June 2008, and confirmation of attendance by RGA, dated 4 July 2008. RGA and European Lotteries were invited by letter of 1 July 2008. The European Commission considers that RGA as a complainant is primarily concerned by the outcome of this investigation, and that also European Lotteries have a sufficiently strong and immediate economic interest in the outcome of this investigation to make them “parties primarily concerned” in the sense of Article 8(6) of the Trade Barriers Regulation. During the hearing, the parties addressed successively the following issues: (1) standing in the case pursuant to Article 4 of the Trade Barriers Regulation (RGA) and Article 8(5) of the Trade Barriers Regulation (European Lotteries); (2) obstacle to trade in the meaning of Article 2(1) of the Trade Barriers Regulation; (3) adverse trade effects caused by the alleged obstacle, its presence or a threat, within the meaning of Article 2(4) and Article 10 of the Trade Barriers Regulation, (4) Community interest. Both parties were given the opportunity for concluding remarks.

In addition, both parties could submit additional written submissions relating to their oral remarks until 25 July 2008. European Lotteries submitted a document with the title “Written Observations Following the Confrontational Hearing on Behalf of the European State Lottery and Toto Association”.

A.5. Initiation of the investigation

The investigation was initiated on 11 March 2008, after the Commission determined that the complaint contained sufficient evidence to justify the initiation of an investigation.²¹

A.6. Conduct of the investigation

This Trade Barriers Regulation investigation has been characterised by the refusal by many private sector operators, notably in the US, to provide information to the Commission services. This attitude of extreme caution on the side of the private sector has significantly hampered the investigation activity. It is obvious that this attitude has

²¹ OJ C 45, 11.3.2008, p. 5

been due to the extreme sensitivity of the matter given the involvement of the US Department of Justice (DOJ) and, more specifically, the fact that DOJ investigations on the supply of remote gambling and betting services in the US are ongoing. This has had an impact on the information made available to the Commission services, in particular as regards details of DOJ enforcement activity against US or EU operators.

During the first stage of the investigation, the Commission services gathered information on the services subject to investigation; on the legislation and its enforcement in the US; on the relevant US, Community and world markets and industries; and on the adverse effects claimed by the complainant. This information has been mainly collected by means of different questionnaires addressed to:

- The complainant;
- Community and US suppliers of remote gambling and betting services, and their associations;
- Community and US suppliers of supporting services to the remote gambling and betting services industry;
- The US government;
- EU Member States concerned.

In response to the invitation contained in the notice of initiation, the Commission services received requests from certain interested parties to be heard in the context of the investigation. Hearings were held, as described in section A.4, with the NASPL; the WLA; European Lotteries; and Stanleybet International. Moreover, a hearing with the complainant and European Lotteries was organised to allow the participants to present opposing views.

After collecting the information referred to above, the Commission services carried out a verification visit to the US (Washington, DC) between 15 and 18 September 2008. Commission officials met with the US government (USTR, DOJ, DOS, DOC and DOT); Members of Congress (Shelley Berkley (D-NV) and Robert Wexler (D-FL)) and congressional staffers to key Committees and/or Members; and private sector interests which it is not appropriate to disclose. It is nonetheless worth noting that individual financial institutions and horseracing interests declined to meet.

The complainant lodged on 24 October 2008 an "Additional Submission on Measures at Issue and Discrimination".

The Commission services wish to remark that in terms of the procedural aspects under the Trade Barriers Regulation, co-operation from the US government throughout this investigation has been in line with the requirements of the Trade Barriers Regulation. The Commission services have taken particular care to ensure that the US government could fully exercise its right of defence with regard to the allegations made by the RGA in the complaint. In exercising its right of defence, the US government has opted for simply refuting the allegations by the RGA and has provided only relatively limited information in support of its position. This is consistent with the long-standing position of the US government that the remote supply of gambling and betting services is prohibited in the US, and that any allegation of "discriminatory enforcement" of US gambling laws is unfounded.

The issuance of the report has been delayed beyond the 7 months deadline provided by Article 8.8 of the Trade Barriers Regulation by two events. First, the unexpected delay of the verification visit to the US. The verification visit was initially foreseen for July 2008. However, in response to the Commission services notification of the visit, the US government objected to the start of this verification visit on 21 July. The US expressed doubts about whether a verification mission was necessary, and requested the Commission services to provide, at least two weeks in advance of any verification mission, a list of the persons or organisations that the Commission intended to meet, as well as, for each such person or organisation, a list of written questions that the Commission intended to ask. The Commission services did not agree to disclose the list of persons or organisations that it intended to meet, but prepared a further questionnaire for the US government. The US agreed to a verification mission on that basis, which finally took place between 15 and 18 September 2008. Second, the US DOT and the Board of Governors of the Federal Reserve System published on 12 November 2008 a joint notice to adopt a final rule to implement applicable provisions of the UIGEA. The notice announced that the final rule would be effective on 19 January 2009, although compliance by the relevant financial entities would not be required until 1 December 2009. This final rule, aimed at prohibiting the funding of unlawful internet gambling, has been analysed and the subsequent conclusions incorporated into this report.

B. FACTUAL BACKGROUND

B.1. The market for gambling and betting services

B.1.1. Size and structure of the market

Complete and accurate data on the gambling and betting sector, and in particular on the remote gambling and betting segment, are not available. However, a number of sources offer sufficient information to provide an approximate picture of the size and structure of the gambling and betting sector, including remote supply.

The "Study of Gambling Services in the Internal Market of the European Union"²² provides useful data. It concludes that "the EU gambling market generated Gross Gambling Revenues (operator winnings, less payment of prizes) of approximately €51,500 million in 2003."²³ This Study also provides a useful comparison of the EU and US markets, describing their main segments in the following way:

"As against the EU figure of approximately €51,500 million in 2003, the legal American gaming industries in 2003 generated Gross Gaming Revenues (GGRs) of US\$72,800 million (€60,700 million). Though aggregate GGRs were similar between the US and EU as of 2003, their composition differed considerably between the European Union Member States as a group and the United States. For example, in the United States, commercial and tribal casinos generated about US\$42,100 million of the total US GGRs in 2003 (58% of the US total), whereas in the EU, casinos comprised only about €7,500 million of

²² Study of Gambling Services in the Internal Market of the European Union. Final Report, 14 June 2006. Swiss Institute of Comparative Law

²³ Ibid., p. xxxvi

GGRs (15% of the EU total.) In the United States, gaming machines (also referred to as slots, Electronic Gaming Devices, or Video Lottery Terminals) outside of casinos are still relatively uncommon; in 2003, such devices generated GGRs of US\$3,900 million (5% of the US total) whereas in the European Union, gaming machines generated GGRs of €9,700 million (19% of the EU total.) Lotteries in the United States generated GGRs of \$17,400 million (excluding Video Lottery Terminals), 24% of US GGRs, whereas in the EU, lottery GGRs were €23,000 million, 45% of the EU total. Betting services, including on-track and off-track betting on horses and sports, amounted to only US\$3,900 million, or 5% of US GGRs, whereas in the EU, the comparable statistic was €8,900 million, 17% of the EU total. Finally, bingo services and charitable gambling generated about US\$4,000 million, or 5% of US GGRs, and in the EU, bingo services were also a relatively small component in the EU, at €2,400 million, or 5% of the EU total."²⁴

The same Study describes the remote gambling and betting segment in the following way:

"Figures published by the River City Group and by the Association of Remote Gambling Operators indicate that the global interactive gambling market currently provides a GGR of about €5,700 million (US\$7,000 million) per annum as of 2003, with the EU share being about €1,630 million (US\$1,980 million). The global remote and internet gaming industry is forecast to grow from about US\$9,000 million in 2004 to US\$25,000 million in 2010. Based upon a review of these studies of remote and internet gaming – as well as survey data collected as a portion of our own Study – the economic research team's best estimate of the size of the European Union remote and internet gaming sector (that sector which offers gambling services via the internet, through mobile phone services, and through interactive television wagering) represented between €2,000 million and €3,000 million in GGRs from EU consumer expenditures in 2004, and growing rapidly. If the above estimates hold true, then the economic importance of remote gambling is likely to continue to rise, but not beyond 5% of the total EU gambling market by 2012. This estimate takes account of both factors favoring growth and factors that could restrict it. In those EU Member States which have poorly developed land-based gaming sectors, the importance of remote gambling as a proportion of the total market for gambling services could rise well beyond 5%."²⁵

This Study offers some other useful insights into the remote gambling market, including with regard to the position of EU companies and the impact on employment. For example, it remarks that, in Malta, "[G]ambling GGR as a percentage of GDP in 2003 was 7.3% compared to the EU average of 0.7%,"²⁶ and concludes that EU companies, especially those with a British base, enjoy a leading position in the world-wide remote gambling and betting market. The Study quotes in this respect research from 2005 showing that the top five remote operators according to this research (William Hill,

²⁴ Ibid., p. xxxvii

²⁵ Ibid., p. xl

²⁶ Ibid., p. 1404

Ladbrokes, Sportingbet (all British), Bwin (Austria) and Cryptologic (Canada)) accounted for 63.3% of the market capitalisation of the "top 30" operators. It further adds that, in 2003, *The Economist* estimated that British companies held around three-quarters of the cross border betting market.²⁷

With regard to the employment levels of remote gaming companies, the same Study includes the following information:

"Remote gaming companies were also queried with respect to their employment levels, in their primary EU country, elsewhere in the EU, and outside the EU. If indeed this cohort of respondents reflects about half the remote gaming industry in the EU, then the employment growth for the sector went from less than 500 in 2000 to around 5,000 in 2004. Forecasts for future employment growth would push total employment (within and outside the EU) to about 10,000, of whom about 6,000 would be employed within the EU. Thus, even though the remote gaming sector may become an increasingly important part of the gambling services sector in the EU, it is likely to remain a relatively small employer.

Based on the survey results, the proportion of employees with remote gaming companies located within the company's primary EU country of operation declined from about 75% in 2000 to around 50% in 2004. Forecasts through 2009 suggest this ratio will fall further, to about 40%. The proportion of employees working elsewhere in the EU ranged between 10% and 15% between 2000 and 2004, and was expected to be around 15% in 2009. Finally, the proportion of employment outside the EU grew from 10% to 40% between 2000 and 2004, and was forecast to stay about 40% through 2009, with negligible amounts of employees based in other EU countries and outside of the EU. Looking forward to 2009, employment within the EU is projected by respondents to grow at an aggregate of five percent each year for the next four years, while employment outside of the EU is estimated to remain somewhat constant, or grow only in proportion to over-all business growth."²⁸

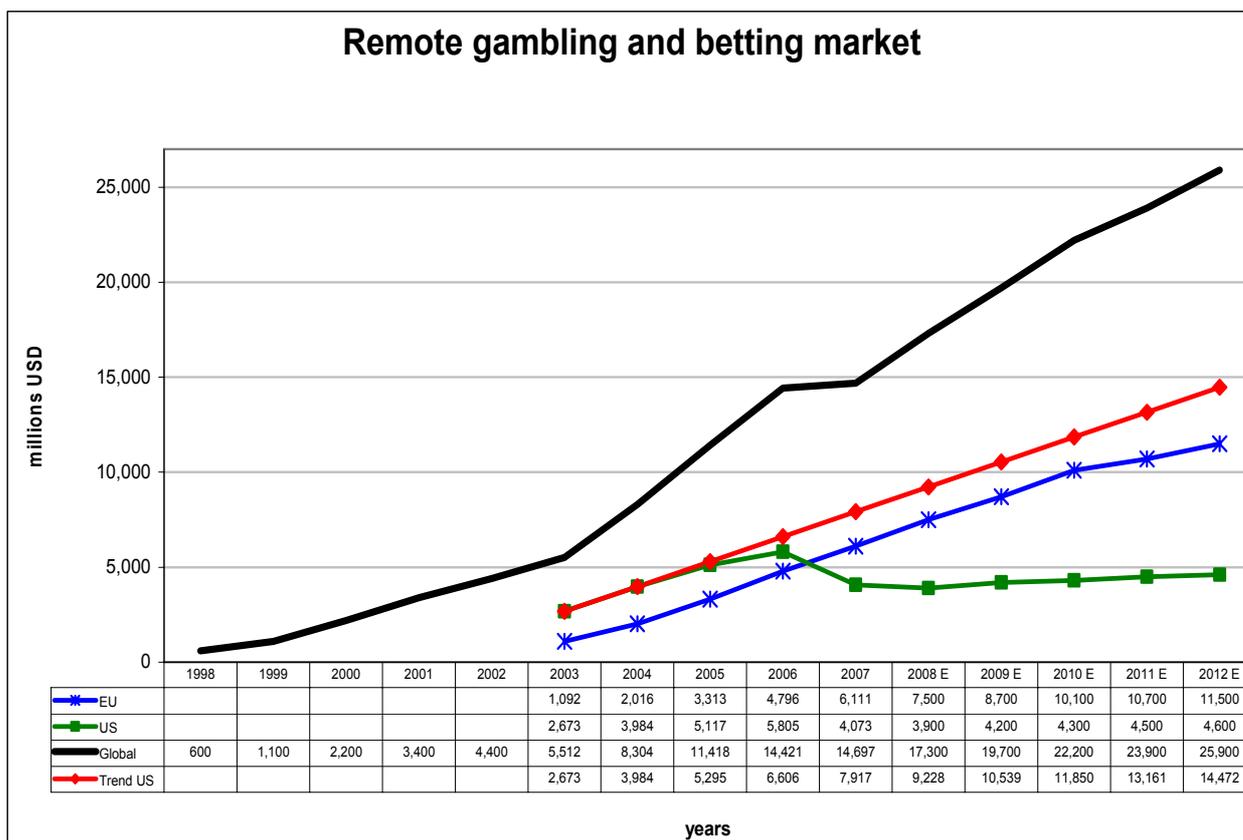
The complaint contained estimates of the number of staff employed by the Internet gaming industry in the EU, provided by a specialised recruitment consultancy to the online gaming industry.²⁹ According to these estimates, over 15,000 staff are employed by the Internet gaming industry in the EU, with a current annual growth rate of 10%. 8,000 employees would be active in the UK; 2,000 in Malta; 2,000 in Gibraltar; 1,500 in Ireland; 500 in Sweden; 500 in Cyprus; 500 in Austria; and 500 in the rest of the EU.

Further data have been made available to the Commission services during this investigation, in particular by the complainant on the basis of industry data. These data can be summarised by means of the following table:

²⁷ Ibid., p. 1405

²⁸ Ibid., p. 1422

²⁹ Statement from BettingJobs.com attached to the complaint as Annex 3



Source: Industry responses and calculations by the Commission services. Figures correspond to "Gross Gaming Yield" (stakes wagered less winnings paid out)

The above table shows the evolution of historical data and future estimates of the remote gambling and betting market worldwide, in the US and in the EU. It not only offers figures reflecting the size of the market from 2003 (and back to 1998 as regards the global market) until 2012, but also provides an estimate of the likely evolution of the US market in the absence of the specific restrictions imposed in 2006, based on an assumption of a 3% yearly growth until 2012.

Remote gambling and betting market (GGY, \$billion)										
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
EU	1.09	2.02	3.31	4.80	6.11	7.50	8.70	10.10	10.70	11.50
US	2.67	3.98	5.12	5.80	4.07	3.90	4.20	4.30	4.50	4.60
World	5.51	8.30	11.42	14.42	14.70	17.30	19.70	22.20	23.90	25.90

It is interesting to consider these figures against the backdrop of estimates of the global market for gambling and betting services, also provided by the complainant in the context of this investigation:

Gambling and betting market (GGY, \$billion)										
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
EU	85.3	96.5	98.3	104.6	111.7	118.6	125.3	131.0	135.5	139.7
US	86.9	98.5	100.1	105.6	109.7	115.0	120.8	125.3	129.3	132.8
US*	72.9	78.8	84.4	90.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
World	253.6	283.0	295.0	310.8	335.2	351.9	363.8	375.0	383.8	391.7

** American Gaming Association Data, excluding online betting*

These data show that the size of the online market is substantial, with estimates of the total size of the world remote gambling and betting market surpassing \$14 billion in 2007, out of a total global market of gambling and betting of 335 billion. Around \$6 billion thereof correspond to the EU online market, while the size of the US online market is estimated at \$4 billion. The total size of the EU gambling and betting market is estimated at \$116 billion, and the US market at \$110 billion. Estimates of the size of the world online market for 2010 surpass \$22 billion.

According to data provided by Malta's government to the Commission services during the investigation, the contribution of the gaming industry to Malta's GDP in 2007 was 5.4%, and 6.3% of the total gross value added of the Maltese economy. Moreover, the sector in Malta had a 12% market share of the industry in 2007, and employed a total of 1,882 staff as of June 2008. These data are consistent both with those figuring in the Study of Gambling Services in the Internal Market of the European Union quoted above, and also with the data on employment offered in the complaint.

According to a study on the impact of online gambling and betting in the economy of Gibraltar, the online gaming sector accounts for 1,689 direct jobs and 2,548 direct and indirect jobs. These data are consistent with the data on employment offered in the complaint.

Data provided by the UK government to the Commission during the investigation show that the gambling and betting sector accounted in the UK in 2006 for almost 2000 companies with a total turnover (excluding VAT) of more than £50 billion (up from £13.9 billion in 1998), an approximate gross value added of £3.9 billion, and over 100,000 employees (up from 76,000 employees in 1998).

The employment estimates for the online gambling and betting sector available to the Commission range between 6,000 jobs according to the "Study on the Study of Gambling Services in the Internal Market of the European Union", and above 15,500 according to the complainant. Given that the figures corresponding to Malta and Gibraltar obtained during the investigation support the data provided in the complaint, it is considered safe to assume a real figure of above 10,000 employees. Moreover, a number of factors are likely to underpin substantial growth in the demand for remote gambling. These factors were referred to in the "Study of Gambling Services in the

Internal Market of the European Union"³⁰, and include the following: increasing penetration of computers, the Internet and broadband connections; development of more user-friendly and increasingly integrated technologies; safer electronic financial transactions; and increase in leisure spending.

Without prejudice to the significant impact that the general economic situation may have on the figures, these factors suggest that it would be justified to expect continued growth of the online gambling and betting market in the next few years.

B.1.2. Regulation in the EU

There is no specific Community legislation governing the gambling and betting sector. The "Study of Gambling Services in the Internal Market of the European Union" includes a "Legal Study" covering the legal situation in the different Member States, as well as an analysis of the relevant jurisprudence, notably from the European Court of Justice.³¹

The recent Progress Report drafted by the French Presidency on the issue³² provides an updated summary description of Member States' rules on gambling and betting services. In particular, it states the following:

"In all the Member States, the various forms of gambling and betting are permitted to varying degrees and are submitted to specific regulation rules. Underlying the legislation of half of the Member States...is the principle that gambling is illegal unless authorised, whereas in other Member States gambling and betting is more open, though regulated. Casino games, slot machines and betting on events other than sporting contests and horse racing are the most frequently restricted forms. The rules on access to online gambling and betting are frequently more restrictive: six Member States ban it entirely...; others, while not going as far as banning it, apply additional restrictions on online gambling, particularly regarding casinos. Another group of member States have introduced open, though regulated, systems.

As far as market structure is concerned, in most Member States the different sectors of the gambling and betting industry (lotteries, sports betting and betting on horse racing, casinos, slot machines, bingo and the other forms of gambling and betting) are governed by different rules. Lotteries are in most cases run as monopolies or under exclusive rights granted to state bodies or private, often non-profit, bodies. In almost half the Member States, betting is subject to a system of licences open to a number of operators, while in a large number of Member States there are restrictions on the number of casinos, where they are situated and who can run them.

³⁰ Study of Gambling Services in the Internal Market of the European Union, page 1401. Final Report, 14 June 2006. Swiss Institute of Comparative Law

³¹ Ibid., p. 1

³² Progress Report – Gambling and betting: legal framework and policies in the Member States of the European Union. Prepared by the Presidency with a view to the Competitiveness Council on 1 and 2 December 2008

Responsibility for regulating the sector usually lies with one or more ministries, often the Ministry of Finance. However, some Member States have a specific body operating under the aegis of the relevant ministry, which is responsible for issuing authorisations and monitoring operators, and some others have an independent authority. Local authorities are also frequently involved in granting licences for gambling and betting premises."³³

There is a further recent description of the Member States' rules applicable to gambling and betting services in a Study commissioned by the European Parliament's committee on Internal Market and Consumer Protection (IMCO).³⁴ This report states that:

"The legislative and regulatory landscape for online gambling in the EU is extremely diverse and rapidly changing. No single EU market exists for online or conventional gambling, and the extent of diversity between Member States is so great that we see no likelihood that a single market will emerge at any time soon. Twenty EU Member States allow online gambling and seven do not. Some, by virtue of recent legislation, have decided deliberately to allow or prohibit online gambling, while others allow or prohibit it "passively" by continuing to apply legislation established, often many years earlier, for conventional gambling. Of the twenty Member States that allow online gambling, thirteen operate a liberalised market, six operate state-owned monopolies and one has licensed a private monopoly."

B.2. Remote supply of gambling and betting services by EU companies

The companies operating in the online segment of the market are important players of the gambling and betting sector. For example, in 2007, Ladbrokes had a total operating income of £1.2 billion (about €1.63 billion at 31 December 2007 exchange rates) of which revenue from remote operations was £423.3 million (€ 574.4 million), and a market capitalisation of £1.9 billion (€2.57 billion); William Hill had a total revenue of £940 million (€1.27 billion), of which revenue from remote operations was £173.7 million (€ 235.7 million), and a market capitalisation of around £2 billion (€2.71 billion); Sportingbet had a total operating income of £119.4 million (€162.03 million) and a market capitalisation of £221.9 million (€301.1 million); Paddypower had a total operating income of €278.9 million, of which revenue from remote operations was €121.8 million, and a market capitalisation of €1.1 billion; 888 Holdings had a total operating income of \$216.9 million (€147.36 million) and a market capitalisation of \$482.9 million (€332.64 million); Partygaming reported net revenues of \$457.8 million (€311.07 million), and a market capitalisation of \$2.37 billion (€1.61 billion); Bwin had total revenues of €336.9 million and a market capitalisation of €650.96 million. These figures correspond to all the operations of the relevant companies, including where appropriate non-online operations.

³³ Ibid., paras. 6 to 8. This Report provides further details on the approach of Member States to regulating the gambling and betting sector, in particular in the Annex entitled "Summary of Delegation's Replies to the Questionnaire."

³⁴ "Online Gambling: Focusing on Integrity and a Code of Conduct for Gambling." Policy Department Economic and Scientific Policy. European Parliament. See in particular Appendix 1 entitled "Online Gambling in and beyond the EU" for a description of the regulatory landscape

Community companies that are members of the RGA provide online sports and non-sports betting services, as well as online casino gaming and online card play services, and have provided these services in the past to customers in the US.

[...]

Detailed information of the respective market shares of these companies in the EU and in the US is considered commercially sensitive, so that very few data on market shares have been made available to the Commission. However, the data at the disposal of the Commission services regarding the revenues obtained by a number of European companies as a result of their operations on the US market,³⁵ as well as the volume of their operations, are consistent with the statement in the complaint that the EU has developed the world's leading Internet gaming business.

C. THE CHALLENGED MEASURES AND OBSTACLES TO TRADE

C.1. Introduction

The complaint summarises the challenged measures as:

- (i) WTO-illegal legislation imposing a ban on Internet gambling;
- (ii) Measures taken to enforce that legislation;
- (iii) The fact that the legislation is enforced in a discriminatory way.

The complaint recalled that the WTO Appellate Body had already found that by maintaining three laws, namely the Wire Act, the Travel Act and the Illegal Gambling Business Act (IGBA), the United States was acting inconsistently with its obligations under Article XVI of the GATS. It further argued that any measures taken to enforce the Wire Act, the Travel Act and the IGBA against foreign service suppliers would also inevitably be contrary to Article XVI. Moreover, by enforcing its laws in a discriminatory way, the US would also be violating Article XVII of the GATS.

The complaint also remarked that the US legal context was complex and unclear, and that it was difficult to make a clear distinction between the law, the interpretation of the law, and application of the law. In order to avoid the need to conduct a debate on the correct interpretation of US law, the complaint focused on the US authorities own interpretation of US law, namely the US Department of Justice belief that current US federal law prohibits all type of gambling over the Internet, including any type of gambling offered by domestic suppliers.

On 24 October 2008, the complainant lodged an "Additional Submission on Measures at Issue and Discrimination", in which it sought to provide further facts and further develop its argumentation regarding the second and third aspects of the complaint (i.e. regarding measures taken to enforce the legislation and the allegation of discriminatory enforcement).

³⁵ See in this respect section on "Adverse Trade Effects" below.

This section will first attempt to summarise the applicable US legal framework, identifying the main areas where its interpretation is unclear or debated. A legal analysis will then seek to, first, identify the measures that could potentially be challenged, and, second, assess whether and to what extent those measures can be considered to be consistent with the US obligations under the GATS. It will finally conclude on whether the measures at stake can be considered to constitute an obstacle to trade within the meaning of the Trade Barriers Regulation.

C.2. The challenged measures: US laws prohibiting cross-border supply but allowing supply within the US

C.2.1. The Wire Act

The complaint refers to the Wire Act (18 U.S.C. § 1084) as the federal statute that applies most "naturally" to Internet gambling, and partially quotes subsection (a) of 18 U.S.C. § 1084. The full quote reads as follows:

"Whoever being engaged in the business of betting or wagering knowingly uses a wire communication facility for the transmission in interstate or foreign commerce of bets or wagers or information assisting in the placing of bets or wagers on any sporting event or contest, or for the transmission of a wire communication which entitles the recipient to receive money or credit as a result of bets or wagers, or for information assisting in the placing of bets or wagers, shall be fined under this title or imprisoned not more than two years, or both."

"Wire communication" is defined in 18 U.S.C. § 1081 in the following way:

"The term "wire communication facility" means any and all instrumentalities, personnel, and services (among other things, the receipt, forwarding, or delivery of communications) used or useful in the transmission of writings, signs, pictures, and sounds of all kinds by aid of wire, cable, or other like connection between the points of origin and reception of such transmission."

The plain wording of 18 U.S.C. § 1084 suggests that it is prohibited to transmit bets or wagers in interstate or foreign trade using a wire communication.³⁶ As a result, the Wire Act is one of the federal laws that prohibit all types of gambling over the Internet. This is the interpretation of the US administration, including in particular the DOJ. This DOJ position was referenced in the complaint,³⁷ and was confirmed by USTR and DOJ at the meeting held with the European Commission on 16 September 2008 in the context of the investigation visit in this Trade Barriers Regulation case. This was also what the Panel

³⁶ The term "wire communication" includes communication by the Internet. This results both from the definition of "wire communication facility" in 18 U.S.C. § 1081 and applicable case law. See in this respect the Panel report, *US-Gambling*, footnote 853

³⁷ E.g. Letter from William E. Moschella, Assistant Attorney General to Rep. John Conyers Jr., OJ, 14 July 2003. This letter also reflected the DOJ opinion that the *Mastercard* case, according to which the Wire Act would only apply to sports betting, was wrongly decided on the law

found in *US-Gambling* as regards the cross border supply of gambling and betting services over the Internet.³⁸

There are, however, two debated questions - referred to in the complaint - in relation to the scope of the Wire Act. First, the question of whether non-sports betting is caught by the Wire Act; and, second, the question of whether Internet horse race betting is given a "safe harbour" from the prohibition of the Wire Act by the Interstate Horse Racing Act. Two further questions, not mentioned in the complaint but relevant for this investigation, are the question of the applicability of the Wire Act to intrastate commerce and the interpretation to be given to subsection (b) of 18 U.S.C. § 1084.

C.2.1.1. Sports betting vs. non-sports betting

The complaint argues that the Wire Act, according to its wording, its legislative history and the available case law (notably a federal Court of Appeals ruling³⁹ of 2002, the highest instance in which this issue has ever been considered), applies only to sports betting and not to betting on non-sports. The complaint even quotes the testimony of a DOJ official⁴⁰ remarking that the Wire Act may relate only to sports betting, and not to e.g. online poker. The GAO report quoted above also remarks that the language of the Wire Act "has led some courts to interpret the Wire Act as covering bets only on contests that involve sports".⁴¹ This was also one of the main reasons why according to the complainant, EU companies offering non-sports gambling over the Internet had been active on the US market.

However, this interpretation is contradicted by the position otherwise adopted by the DOJ and the US administration more generally, that current federal law prohibits all types of gambling over the Internet, as indicated above.⁴²

C.2.1.2. The Interstate Horse Racing Act

According to the complaint, US based operators of Internet horse race betting consider the Interstate Horse Racing Act (IHA) – as amended in December 2000 - to provide a "safe harbour" from the Wire Act. This was also the view taken by a number of private operators who provided input in this investigation, and is notably the view of the US National Thoroughbred Racing Association.⁴³ The GAO report on Internet gambling also

³⁸ Panel Report, *US-Gambling*, para. 6.362

³⁹ *Mastercard*, US Court of Appeals for the Fifth Circuit, 20 November 2002

⁴⁰ Testimony of Kevin V. Di Gregory, Deputy Assistant Attorney General, DOJ, 9 June 1999

⁴¹ See p. 12 in "Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002

⁴² One should nonetheless note that Antigua did not argue before the *US Gambling* Panel that the Wire Act did not apply to non-sports betting, but rather the opposite: that the relevant federal laws imposed the equivalent of a zero quota for cross-border supply of gambling and betting services

⁴³ "The legislation (UIGEA) contained language that recognizes the ability of the horse racing industry to offer account wagering under the IHA of 1978 as amended..." National Thoroughbred Racing Association, press release 30 September 2006 "Congress Affirms Horse Racing's Position in Internet Gaming; Legislation Passed by both Houses Early this Morning"

notes in respect of the IHA that "the language of the statute appears to allow the electronic transmission of interstate bets as long as the appropriate consent is obtained....In addition, IHA was amended in December 2000 to explicitly expand interstate off-track wagers to include wagers through the telephone or other electronic media."⁴⁴

The US administration, however, and the DOJ in particular, disagree with this interpretation and maintain that the IHA provides no exemptions or defences to violations of federal criminal laws such as the Wire Act. This position of the US administration was confirmed to the European Commission at the meeting held on 16 September 2008 in the context of the investigation visit to the US in this Trade Barriers Regulation case.

The Panel in *US-Gambling* agreed with Antigua that the text of the IHA does appear, on its face, to permit interstate wagering over the Internet. And even if it the IHA did not repeal the Wire Act, the Panel considered the ambiguity in the relationship between the IHA and the Wire Act (and other federal laws) an essential factor to finding against the US in this case.⁴⁵ The Appellate Body upheld this finding of ambiguity.⁴⁶

Relevant parts of the IHA provide as follows:

15 U.S.C. § 3001 (Congressional findings and policy), subsection (a):

"The Congress finds that –

(1) the States should have the primary responsibility for determining what forms of gambling may legally take place within their borders;

(2) the Federal Government should prevent interference by one State with the gambling policies of another, and should act to protect identifiable national interests; and

(3) in the limited area of interstate off-track wagering on horseraces, there is a need for Federal action to ensure States will continue to cooperate with one another in the acceptance of legal interstate wagers."

15 U.S.C. § 3001 (Congressional findings and policy), subsection (b):

"It is the policy of the Congress in this chapter to regulate interstate commerce with respect to wagering on horseracing, in order to further the horseracing and legal off-track betting industries in the United States."

15 U.S.C. § 3002 (Definitions):

⁴⁴ See p. 16 in "Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002

⁴⁵ Panel Report, *US-Gambling*, paras. 6.599 and 6.600

⁴⁶ Appellate Body Report, *US-Gambling*, paras. 364 and 366

"interstate off-track wager" means a legal wager placed or accepted in one State with respect to the outcome of a horserace taking place in another State and includes pari-mutuel wagers, where lawful in each State involved, placed or transmitted by an individual in one State via telephone or other electronic media and accepted by an off-track betting system in the same or another State, as well as the combination of any pari-mutuel wagering pools;"

C.2.1.3. Intrastate commerce

The main question in respect of intrastate commerce is whether the prohibitions in the Wire Act cover intrastate commerce or not. It appears evident that 18 U.S.C. § 1084 does not, on its face, apply to intrastate commerce given that it refers to only "interstate and foreign trade".

The report by the Panel following Antigua's recourse to Article 21.5 of the Dispute Settlement Understanding (DSU) addressed this factual issue,⁴⁷ which had not been addressed by the original Panel given the focus of Antigua's case on the differential treatment between non-remote gambling within the domestic US market and remote gambling from outside the US. According to the 21.5 *US-Gambling* Panel, it is undisputed that the Wire Act does not prohibit remote wagering within the United States to the extent that it is not in interstate or foreign commerce. Moreover, it pointed out that, according to Antigua's submissions, "there are at least 18 State laws (laws outside the Panel's terms of reference) that expressly authorize wagering by wire within the United States, including on a wholly intrastate basis".⁴⁸

The role of state laws is addressed in more detail in the relevant section below.

C.2.1.4. The interpretation of subsection (b) of 18 U.S.C. § 1084

Subsection (b) of 18 U.S.C. § 1084 provides as follows:

"(b) Nothing in this section shall be construed to prevent the transmission in interstate or foreign commerce of information for use in news reporting of sporting events or contests, or for the transmission of information assisting in the placing of bets or wagers on a sporting event or contest from a State or foreign country where betting on that sporting event or contest is legal into a State or foreign country in which such betting is legal."

According to the GAO report, this implies that transmitting information to assist in placing bets on a certain event is legal if two conditions are met: betting on the event is legal in both the place where the transmission originates and the place where it is received, and the transmission is limited to information but does not include the bet itself. Certain courts have understood this as allowing interstate gambling. However, most courts disagree with this interpretation and, based upon its language and clear statements in the legislative history, the DOJ disagrees as well.⁴⁹

⁴⁷ 21.5 Panel Report, *US-Gambling*, paras. 6.93 to 6.97 and 6.118 to 6.123

⁴⁸ 21.5 Panel Report, *US-Gambling*, para. 6.121

⁴⁹ See p. 13, "Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002.

C.2.2. *The Travel Act*

The complaint refers to the prohibition in the Travel Act to use any facility in interstate or foreign commerce with intent to participate in unlawful activities, including any business enterprise in violation of State or US laws. It underlines the fact that the applicability of the Travel Act depends on the applicability of state law or other federal laws.

Relevant parts of the Travel Act provide as follows:

18 U.S.C. § 1952 (Interstate and foreign travel or transportation in aid of racketeering enterprises), subsection (a):

Whoever travels in interstate or foreign commerce or uses the mail or any facility in interstate or foreign commerce, with intent to -

(1) distribute the proceeds of any unlawful activity; or

(2) commit any crime of violence to further any unlawful activity; or

(3) otherwise promote, manage, establish, carry on, or facilitate the promotion, management, establishment, or carrying on, of any unlawful activity, and thereafter performs or attempts to perform -

(A) an act described in paragraph (1) or (3) shall be fined under this title, imprisoned not more than 5 years, or both; or

(B) an act described in paragraph (2) shall be fined under this title, imprisoned for not more than 20 years, or both, and if death results shall be imprisoned for any term of years or for life.

18 U.S.C. § 1952 (Interstate and foreign travel or transportation in aid of racketeering enterprises), subsection (b):

"As used in this section (i) "unlawful activity" means (1) any business enterprise involving gambling, liquor on which the Federal excise tax has not been paid, narcotics or controlled substances (as defined in section 102(6) of the Controlled Substances Act), or prostitution offenses in violation of the laws of the State in which they are committed or of the United States (...)"

On its face, the Travel Act prohibits the use of any facility in interstate or foreign travel in relation to gambling by an enterprise in violation of state or federal laws. It thus depends on the applicability of other state or federal laws.

The Panel in *US-Gambling* interpreted the Travel Act as prohibiting gambling activity that entails the supply of gambling and betting services by mail or any facility to the extent that such supply is undertaken by a business enterprise involving gambling in violation of state or US law.⁵⁰

⁵⁰ Panel report, *US-Gambling*, para. 6.367

C.2.2.1. Intrastate commerce

The question of whether intrastate commerce is covered by the prohibitions in the Travel Act is also relevant. As in the case of the Wire Act, the text of 18 U.S.C. § 1952 shows that its scope is limited to interstate and foreign commerce, given that it includes no reference to "intrastate commerce".

This was also the view expressed by the Panel in the report following Antigua's recourse to Article 21.5 DSU in the *US Gambling* case.⁵¹

C.2.3. *The Illegal Gambling Business Act (IGBA)*

The IGBA provides as follows:

18 U.S.C. § 1955 (Prohibition of Illegal Gambling Businesses), subsection (a):

"Whoever conducts, finances, manages, supervises, directs, or owns all or part of an illegal gambling business shall be fined under this title or imprisoned not more than five years, or both."

18 U.S.C. § 1955 (Prohibition of Illegal Gambling Businesses), subsection (b):

"As used in this section -

(1) "illegal gambling business" means a gambling business which -

(i) is a violation of the law of a State or political subdivision in which it is conducted;

(ii) involves five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such business; and

(iii) has been or remains in substantially continuous operation for a period in excess of thirty days or has a gross revenue of \$2,000 in any single day.

(2) "gambling" includes but is not limited to pool-selling, bookmaking, maintaining slot machines, roulette wheels or dice tables, and conducting lotteries, policy, bolita or numbers games, or selling chances therein.

(3) "State" means any State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, and any territory or possession of the United States."

On its face, the IGBA prohibits the operation of any illegal gambling business, which is defined as a gambling business which is in violation of the law of the state (or other political subdivision) in which it is conducted. As remarked in the complaint, the IGBA thus turns ultimately on state law and on the question of where the gambling business is conducted.

⁵¹ 21.5 Panel report, *US-Gambling*, para. 6.119

This was also the conclusion of the Panel in *US-Gambling*, according to which IGBA "effectively prohibits the supply of gambling and betting services through at least one and potentially all means of delivery included in mode 1" by gambling businesses defined as illegal in the relevant state laws.⁵²

C.2.4. *The Unlawful Internet Gambling Enforcement Act (UIGEA)*

UIGEA was enacted in October 2006 with the purpose of prohibiting the funding of unlawful Internet gambling. According to the complainant, prior to the adoption of UIGEA, there existed no federal statutory or regulatory framework specifically addressing Internet gambling – even though some federal laws had indeed been deemed to apply to remote gambling and betting services. It is important to note that, at least according to the face of the law, UIGEA does not seek to define or modify the definition of what constitutes unlawful Internet gambling in the United States. This was also the explanation of UIGEA provided by the US administration in the context of this investigation. The US administration indicated that UIGEA did not change which gambling activities are lawful or unlawful, but rather provides for enhanced enforcement mechanisms.

UIGEA provides as follows:

31 U.S.C. § 5361 (Congressional findings and purpose), subsection (b):

"Rule of Construction. - No provision of this subchapter shall be construed as altering, limiting, or extending any Federal or State law or Tribal-State compact prohibiting, permitting, or regulating gambling within the United States."

However, the complaint argues that the enactment of UIGEA significantly altered the regulatory framework applicable to Internet gambling, and this in at least two respects:

- First, because the applicability of state law to out-of-state gambling businesses before UIGEA was unclear. There was no federal legislation on the matter, and the case law on the question of the location of the wagering or the gambling business was inconclusive. As a result, it was unclear whether e.g. a foreign Internet gambling operator accepting bets from a US state was in violation of that state's laws. However, the definition of "unlawful Internet gambling" in UIGEA makes it clear that state law becomes applicable for the purposes of UIGEA as soon as a bet or wager is "initiated, received or otherwise made".

The UIGEA definition is as follows:

31 U.S.C. § 5362 (Definitions):

"(10) Unlawful internet gambling. -

(A) In general. - The term "unlawful Internet gambling" means to place, receive, or otherwise knowingly transmit a bet or wager by any means which involves the use, at least in part, of the Internet where such bet or wager is

⁵² Panel report, *US-Gambling*, para. 6. 375

unlawful under any applicable Federal or State law in the State or Tribal lands in which the bet or wager is initiated, received, or otherwise made."

- Second, as a result of UIGEA's impact on the so-called "dormant commerce clause", which limits the states' ability to restrict trade across state borders. According to Article 1, Section 8, Clause 3 of the US Constitution, Congress shall have the power "to regulate commerce with foreign nations, and among the several states, and with the Indian tribes." The GAO report indicates that "[A]lthough gaming regulation is essentially left to the states, the federal government has the authority, under the Commerce Clause of the Constitution, to regulate gambling activity that affects interstate commerce."⁵³ Based on this "commerce clause", a negative "dormant commerce clause", according to which states cannot pass legislation that imposes improper burdens or discriminations in interstate commerce, has been developed through case law in the US. By adopting UIGEA, including its definition of "unlawful Internet gambling", Congress could have modified the relevance of the "dormant commerce clause" in respect of Internet gambling.

Moreover, and even if the UIGEA did not modify the situation as regards what constitutes unlawful Internet gambling, it can still shed some light on what exactly is allowed and what is prohibited in this respect in the US. The UIGEA explicitly excludes from the definition of unlawful Internet gambling intrastate transactions, intratribal⁵⁴ transactions and activities allowed under the IHA.⁵⁵

More specifically, and with respect to intrastate and intratribal transactions, UIGEA imposes age and location verification requirements designed to block access to minors and persons located out of the relevant State, as well as appropriate security standards to prevent access by any person whose age and location have not been verified. With respect to interstate horseracing, UIGEA excludes any activity that is allowed under the IHA.

The logical implication of these exclusions, and given the nature of the UIGEA as a law intended to enforce all existing prohibitions against Internet gambling, is that the transactions excluded from the scope of the UIGEA are, indeed, allowed. However, the US administration denied in its contribution to this investigation that UIGEA would suggest or imply that certain gambling activities would be permitted in the US. This position of the US administration was to be expected, and is consistent with the view that the passing of the UIGEA – at the very least - confirms that there is an ambiguity, which the UIGEA does not seek to alter, as regards which activities related to horse racing may

⁵³ See p. 12 of "Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002

⁵⁴ I.e. within the Indian lands of a single Indian tribe or between the Indian lands of 2 or more Indian tribes to the extent that Intertribal gaming is authorized by the Indian Gaming Regulatory Act (25 U.S.C. 2701 et seq.) and in compliance with the applicable tribal ordinance or resolution and, if appropriate, the applicable Tribal-State Compact. This report will not conduct any specific analysis regarding gambling within or between Indian lands, in the understanding that this type of gambling could not go beyond what the rules otherwise allow for remote intrastate and interstate gambling. As remarked in 25 U.S.C. 2701, "Indian tribes have the exclusive right to regulate gaming activity on Indian lands if the gaming activity is not specifically prohibited by Federal law and is conducted within a State which does not, as a matter of criminal law and public policy, prohibit such gaming activity."

⁵⁵ 31 U.S.C. § 5362 (10) (B), (C), (D)

or may not be allowed under Federal law, and the relationship between IHA and other federal laws.⁵⁶

The 21.5 Panel in *US-Gambling* addressed the UIGEA,⁵⁷ pointing at the fact that its definition of "unlawful Internet gambling" excludes certain activities and that, as regards interstate transactions under the IHA, in enacting UIGEA the US Congress appears to have contemplated that some activity may be allowed under the IHA that might otherwise be considered "unlawful Internet gambling". However, the 21.5 Panel in the end simply concluded that, by enacting the UIGEA, the US had enacted legislation confirming the ambiguity that had led the original Panel to find against the US.

C.2.4.1. UIGEA implementing rules

On 1 October 2007, the US Department of the Treasury and the Board of Governors of the Federal Reserve System issued a Federal Register Notice proposing rules to implement the mandate contained in UIGEA⁵⁸ to prescribe regulations requiring designated payment systems to block restricted transactions. Although the UIGEA established a period of 270 days for the relevant agencies to prescribe these regulations, the final rules had not yet been published at the time of the Commission services verification visit to the US. The US administration did not provide any indication in the context of this investigation as to when the final rules would be published.

The draft rules required participants in payment systems that could be used in connection with unlawful Internet gambling to establish policies and procedures to prevent transactions in connection with unlawful Internet gambling. The proposed rule did not specify which gambling activities or transactions were legal or illegal, because the UIGEA itself deferred to the underlying laws in that regard. However, the Federal Register Notice requested comments on the possibility of creating a list of unlawful Internet gambling businesses. This was considered by the responsible agencies as a highly complex task which would require the responsible agencies to formally interpret the various applicable federal and state gambling laws. This analysis would be further complicated by the fact that the legality of a particular Internet gambling transaction might change depending on the location of the gambler and the location where the bet or wager was received. It is worth noting that these difficulties highlighted in the Federal Register Notice seem to assume that certain Internet gambling transactions are indeed allowed, in contradiction with the official position of the US administration that all types of Internet gambling are prohibited in the US.

The prevailing view of operators that have contributed to this investigation and that would be required to block transactions in accordance with the UIGEA is that the requirement to block transactions could not be implemented without the establishment of a list. Such a list would provide operators with clarity as to which transactions should be blocked. This would not otherwise be possible given the uncertainty regarding what constitutes "unlawful Internet gambling" in the US. Establishing such a list was in turn

⁵⁶ 31 U.S.C. § 5362 (10) (E) (iii)

⁵⁷ 21.5 Panel Report, *US-Gambling*, paras. 6.130 to 6.135

⁵⁸ 31 U.S.C. § 5364

considered to be an impossible task by some of the operators contributing to this investigation.

The Federal Register Notice invited comments until 12 December 2007. Commenters expressed certain views and opinions that are worth recording in this report:

- The uncertainty regarding the definition of what constitutes "unlawful Internet gambling" and the conflicting views about the interpretation of the regulatory framework are presented as fundamental problems that prevent implementation of the UIGEA.⁵⁹
- Commenters generally express a preference for a list of unlawful Internet gambling businesses being established, albeit recognising the major difficulties that would be involved in putting it together.⁶⁰
- The American Horse Council (AHC) comments on the Federal Register Notice reflect the understanding of the horse racing industry in the US that Internet gambling on horse racing, including on an interstate basis, is indeed allowed. This is important, given that, according to their submission, "the AHC includes over 150 equine organizations representing all horse breeds and virtually every segment of the horse industry, including horse owners, breeders, racing organizations, breeding organizations, race tracks, trainers' organizations, veterinarians and farriers". National Thoroughbred Racing Association comments follow similar lines.⁶¹

⁵⁹ See e.g. comments by the American Bankers Association at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&d=TREAS-DO-2007-0015-0110.1>, according to which "The Prohibition does not specify which transactions qualify as "unlawful Internet gambling." Instead, the Prohibition looks to "underlying substantive State and Federal gambling laws and not . . . a general regulatory definition" to determine the scope of what unlawful Internet gambling comprises. ABA believes that requiring banks to be arbiters of gambling laws for all states, as well as federal gambling laws, is infeasible and would place a crippling processing burden and unbounded litigation risk on the nation's payments system participants. Furthermore, the conflict between the Department of Justice and the Agencies on the scope of "unlawful Internet gambling" sows added confusion over what transactions are indeed subject to the Prohibition. By its terms, the Prohibition "exempts three categories of transactions" from what "unlawful Internet gambling" appears to be: (1) intrastate transactions; (2) intratribal transactions; and (3) interstate horseracing transactions. Additionally, according to the Department of the Treasury, "[s]ince the proposed rule only covers "unlawful internet gambling," it in no way requires participants to prevent or prohibit transactions that are lawful under the Interstate Horseracing Act and all other applicable federal statutes." However, the Department of Justice "interprets existing federal statutes . . . as pertaining to and prohibiting Internet gambling. These statutes pertain to more than simply sports wagering." Since the Department of Justice "has consistently taken the position that the interstate transmission of bets and wagers, including bets and wagers on horse races, violates Federal law," no clear authority exists as to which interpretation banks should follow when implementing the Prohibition. If the federal agencies themselves cannot agree on the law, what hope is there that banks can resolve these confounding legal issues?"

⁶⁰ See e.g. comments by Citibank in this respect at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=0900006480379382>, according to which "the issuance of lists would be extremely useful to System participants..."

⁶¹ "The NTRA is a non-profit trade association representing more than 75 United States pari-mutuel Thoroughbred horseracing tracks and advance deposit wagering service providers that collectively handle approximately 85 percent of all monies wagered on U.S. Thoroughbred horse races. As such, the subject addressed by the proposed rule is of vital importance to the NTRA and the horseracing industry. Internet-based wagers placed on pari-mutuel horseracing, as authorized under the Interstate Horseracing Act of 1978 (15 U.S.C. 3001 et seq.) (IHA), are a significant and rapidly growing portion of the state licensed and

The AHC makes the following statements as part of its comments:

"Pari-mutuel wagering on horse racing is licensed and regulated in over forty states. It is wagering, including simulcast wagering and advance deposit wagering, that supports this industry and its underlying agri-business. In the last 25 years interstate wagering, and particularly advance deposit wagering through various forms of electronic media, including the Internet, have grown dramatically. This growth has been pursuant to state law and the Interstate Horseracing Act ("IHA"). Indeed such wagering now represents over 80% of the amount wagered on horse racing in the U.S. For this reason, these forms of wagering, and therefore the proposed regulations, are critical to the racing industry.

Congress recognized the long-standing existence of these forms of wagering and their importance to the state-licensed and regulated horse racing industry when it enacted UIGEA with an exemption from the Act's prohibitions for "any transaction allowed under the Interstate Horseracing Act.

As the rule proposal notes, Section 5362(10) of the Act excludes three forms of wagering from the definition of unlawful Internet wagering, including "any activity that is allowed under the Interstate Horseracing Act of 1978." Therefore, such wagering on horse racing falls outside the prohibitions of the Act."

- Some of the commenters, especially representing State-level interests, express their concern about the implementing rules resulting in an "overblocking" of (lawful, notably relating to interstate Internet gambling on horse racing) transactions. In this context, the Nevada Pari-Mutuel Association argues that the draft implementing rules have not met their mandate because they do not ensure that lawful transactions – notably relating to interstate horse racing - will not be blocked. It is also interesting to note the view of US state lotteries that the use of the Internet in their business is allowed under US law.⁶²

In this respect, the National Association of Provincial Lotteries (NASPL) commented the following:

"The Act prohibits the knowing acceptance by gambling businesses of credit, electronic fund transfers, checks and certain other forms of payment in connection with unlawful Internet gambling by another person. The term "unlawful Internet gambling" expressly excludes a "bet or wager...initiated and received or otherwise made exclusively within a single State" as long as the bet "is expressly authorized by and placed in accordance with the laws of such State" and State law or regulations include age and location verification requirements and security standards designed to prevent wagering by minors and persons located out of such State. 31 U.S.C. 5362(10) (B). Thus, the Act

regulated transactions engaged in by our industry. In recognition of this, the statutory language of UIGEA requires that the regulations being issued under this rulemaking ensure that these transactions not be blocked or otherwise prevented." See NTRA comments at <http://www.regulations.gov>

⁶² See <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=09000064803708b8> comments at

permits individual States to allow their State lotteries to use the Internet as a means of commerce within their state."

- Internet gambling on Greyhound racing is considered by commenters as being equivalent to Internet gambling on horse racing, and therefore also as a lawful activity. In this respect, "American Greyhound Racing Inc." comments that "Pari-mutuel betting, account wagering, and common pool wagering is lawful in several States including New York, Connecticut, Oregon, Kentucky, California, Virginia, New Jersey and Pennsylvania. These transactions use the Internet, and are authorized and regulated without regard to whether the race meet is a horse race or a greyhound race. In fact the only difference between a horse race and a greyhound race is the animal. The technology is identical for each. Moreover, at many horse tracks, there are greyhound races simulcasted and vice versa. The final regulation must address the substantial risk of overblocking these legal transactions, which is in violation of the (UIGEA)".⁶³ It is worth noting that American Greyhound Racing Inc. describes substantial – by no means hidden – operations.⁶⁴ Other operators express similar views and concerns,⁶⁵ including the US association of greyhound racing operators (AGTOA).

Quite unexpectedly, the DOT and the Federal Reserve published on 12 November 2008 a notice to adopt the final rule to implement applicable provisions of the UIGEA,⁶⁶ under the title "Prohibition of Funding of Unlawful Internet Gambling". The final rule "is effective January 19, 2009" but "compliance by non-exempt participants in designated payment systems is not required until December 1, 2009."⁶⁷

The final rule is a lengthy document that sets out a number of definitions; designates payment systems covered by the rule, and exempts certain participants in certain

⁶³ See _____ comments _____ at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=090000648036f09f>

⁶⁴ "Our operations, comprising of Phoenix Greyhound Park, Apache Greyhound park, AZ Off-track Betting Network, and Max's Sports and Simulcasting Wagering Center, are conducted in Phoenix, AZ, Glendale, AZ, Apache Junction, AZ, and various other cities in Maricopa County, having been in business well over 50 years. We currently conduct greyhound racing 362 days a year with an average of 15 races per day, which we export to over 25 states and countries on a daily basis, as well as importing numerous races from other pari-mutuel facilities throughout the country. We employ over 400 people throughout the Phoenix Metropolitan area and in other parts of the State of Arizona.". Comments at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=090000648036f09f>

⁶⁵ See comments by Greene Group Inc., with greyhound racing operations in Texas and Idaho, at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=09000064803633ab>, Tucson Greyhound Park in Arizona at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=0900006480363368>, or comments by Sport View Television Corporation at <http://www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=090000648036335f> adding Louisiana and California to the list of States by "American Greyhound Racing" that allow Internet wagering on horse and dog racing. AGTOA indicates that "greyhound racing (as does horse racing) relies upon State authorised pari-mutuel Internet and account wagering to facilitate the making of bets or wagers on State sanctioned races."

⁶⁶ Final rule available at <http://www.treas.gov/press/releases/reports/unlawfuinternetgambling11.12.08.pdf>

⁶⁷ Final rule - Prohibition of Funding of Unlawful Internet Gambling, p. 2

designated payment systems; requires those that are not exempted to implement certain procedures to prevent restricted transactions; and provides some examples of procedures that those covered by the rule can implement in order to be deemed to meet their obligation of having policies and procedures in place to prevent restricted transactions. In summary, what the final rule does is to impose on the financial institutions covered the obligation to conduct a "due diligence procedure" with respect to commercial customers (but not with regard to individual gamblers) wishing to open accounts, in order to ascertain whether the commercial customers are involved in "unlawful Internet gambling" and, as a method of blocking transactions, the implementation of a code system through transaction codes and merchant/business category codes for cards.

The final rule does not contemplate the establishment or publication of a list of businesses known to be involved in unlawful internet gambling.⁶⁸ Among the reasons provided in the supplementary information in the notice for not establishing such a list, it is argued that UIGEA itself does not set out the precise activities covered by the term "unlawful internet gambling", and that creating such a list would require the relevant agencies to formally interpret the applicable federal and state laws. These interpretations might not be determinative in defining UIGEA's legal coverage and "could set up conflicts or confusion with interpretations by the entities that actually enforce those laws."⁶⁹

Moreover, the final rule does not define "unlawful Internet gambling". The reasons provided for this in the supplementary information provided in the notice include "that a single, regulatory definition of "unlawful Internet gambling" would not be practical. As explained in the notice itself:

"The Act's definition of "unlawful Internet gambling" relies on underlying Federal and State gambling laws. The States have taken different approaches to the regulation of gambling within their jurisdictions and the structure of State gambling law varies widely, as do the activities that are permitted in each State. Accordingly, the underlying patchwork legal framework does not lend itself to a single regulatory definition of "unlawful Internet gambling." The Agencies have attempted to address the payments industry's desire for more certainty that would result from a precise regulatory definition of "unlawful Internet gambling" through the due diligence guidance provided in § ___.6(b). The suggested due diligence process relies on State regulation of Internet gambling and imposes the burden of proof of legality of Internet gambling activities on the gambling business, rather than the designated payment systems and their participants."

Beyond the well known fact that there does not seem to be a clear definition of "unlawful Internet gambling", this explanation is striking because, contrary to what the DOJ has consistently argued, it suggests that Internet gambling activities can be legal in the US.

Still, the supplementary information provided in the final rule comments that "questions regarding what constitutes unlawful Internet gambling should be resolved pursuant to the

⁶⁸ Ibid., p. 9-10

⁶⁹ Ibid., p. 10

applicable Federal and State gambling laws."⁷⁰ Moreover, the relevant agencies take advantage of the supplementary information to suggest that certain games that could be deemed not to constitute "games of chance" because they require skill and could thus be considered to be excluded from "unlawful Internet gambling", could still fall under the UIGEA ("even if chance is not the predominant factor in the outcome of a game, but was still a significant factor, the game could still be deemed to be a "game subject to chance" under a plain reading of the Act.")⁷¹

As far as this investigation is concerned, the most interesting aspect of the final rule is the inclusion in § ____.6(b) of a specific process that the financial entities affected by the rule "could choose to follow to conduct adequate due diligence of commercial customers with respect to the risk of unlawful Internet gambling." This process "would leave the primary responsibility for determining what is lawful and unlawful gambling activity with the State gambling commissions and other gambling licensing activities."⁷² Based on their due diligence, the relevant financial entities would, in the context of their account-opening procedures, either be able to determine that the risk of the commercial customer engaging in an Internet gambling business is minimal, or not be able to determine that such risk is minimal. In the latter case, the financial entity would have two options: either obtaining from the commercial customer a certification that it does not engage in an Internet gambling business, or what is foreseen in § ____.6(b)(2)(ii)(B) of the final rule, which reads as follows:

"(B) If the commercial customer does engage in an Internet gambling business, each of the following –

(1) Evidence of legal authority to engage in the Internet gambling business, such as --

(i) A copy of the commercial customer's license that expressly authorizes the customer to engage in the Internet gambling business issued by the appropriate State or Tribal authority or, if the commercial customer does not have such a license, a reasoned legal opinion that demonstrates that the commercial customer's Internet gambling business does not involve restricted transactions; and

(ii) A written commitment by the commercial customer to notify the participant of any changes in its legal authority to engage in its Internet gambling business.

(2) A third-party certification that the commercial customer's systems for engaging in the Internet gambling business are reasonably designed to ensure that the commercial customer's Internet gambling business will remain within the licensed or otherwise lawful limits, including with respect to age and location verification."

⁷⁰ Ibid., p. 18

⁷¹ Ibid., p. 19

⁷² Ibid. p. 40

The language in § ___.6(b)(2)(ii)(B), on its face, suggests that, contrary to what the DOJ has consistently argued, it is indeed possible to lawfully supply Internet gambling in the US, on the basis of a license, or even, in some cases, without a license.

C.2.5. Other federal laws

C.2.5.1. The Professional and Amateur Sports Protection Act (PASPA)

Enacted in 1992, this law (18 U.S.C. § 3701 et seq.) prohibits States to legalize any gambling on sports. The law is not limited to interstate operations, as the Wire Act is, but covers any type of sports betting. However, it includes some exceptions that were intended to grandfather some specific betting on sports that was taking place at the time of its enactment (18 U.S.C. § 3704). As a result of these grandfathering provisions, the sports lotteries in Oregon and Delaware are exempted, as well as the licensed sports pools in Nevada.⁷³ It is worth noting that pari-mutuel animal racing and jai alai games are also excluded from the coverage of the PASPA (18 U.S.C. § 3704 (a) (4)).⁷⁴

The key provision of the PASPA reads as follows:

18 U.S.C. § 3702 (Unlawful sports gambling):

"It shall be unlawful for -

(1) a governmental entity to sponsor, operate, advertise, promote, license, or authorize by law or compact, or

(2) a person to sponsor, operate, advertise, or promote, pursuant to the law or compact of a governmental entity, a lottery, sweepstakes, or other betting, gambling, or wagering scheme based, directly or indirectly (through the use of geographical references or otherwise), on one or more competitive games in which amateur or professional athletes participate, or are intended to participate, or on one or more performances of such athletes in such games."

C.2.5.2. Interstate transportation of wagering paraphernalia Act (ITWA)

The ITWA (18 U.S.C. § 1953) makes it unlawful (except by a common carrier in the usual course of its business) to carry or send in interstate or foreign commerce any record, paraphernalia, ticket, certificate, bills, slip, token, paper, writing, or other device used, or to be used, or adapted, devised, or designed for use in (a) bookmaking; or (b) wagering pools with respect to a sporting event; or (c) in a numbers, policy, bolita, or similar game. The prohibitions do not apply when in relation with legal gambling or betting. The purpose of ITWA is therefore to restrict the availability of materials and devices used in illegal gambling, so that its applicability is dependent on the violation of a law specifically prohibiting gambling and betting.

⁷³ According to information supplied by the World Lottery Association (WLA) and the North American Association of State and Provincial Lotteries (NASPL), the Oregon and Delaware lotteries do not offer sports betting.

⁷⁴ This may explain why dog racing interests consider any exceptions applicable to horse racing to be relevant for dog racing as well.

C.2.5.3. Legislation on money laundering

18 U.S.C. § 1956 (laundering of monetary instruments) and 1957 (Engaging in monetary transactions in property derived from specified unlawful activity) as well as 18 U.S.C. § 1960 (Prohibition of unlicensed money transmitting businesses) are targeted at preventing the laundering of money related to an unlawful activity. Their applicability is dependent on the violation of a law specifically prohibiting gambling and betting.

C.2.5.4. Racketeer Influenced and Corrupt Organizations Act (RICO Act)

The RICO Act (18 U.S.C. § 1961 et seq.) was enacted in 1970 in order to fight organized crime, but is also used against activities that do not correspond to organized crime as such. Organized crime is in any event not defined in the RICO Act, which defines "racketeering" as follows:

18 U.S.C. § 1961 (Definitions)

"As used in this chapter -

(1) "racketeering activity" means (A) any act or threat involving murder, kidnapping, gambling, arson, robbery, bribery, extortion, dealing in obscene matter, or dealing in a controlled substance or listed chemical (as defined in section 102 of the Controlled Substances Act), which is chargeable under State law and punishable by imprisonment for more than one year; (B) any act which is indictable under any of the following provisions of title 18, United States Code:...section 1084...section 1953, 1955...1956...1957...1960..."

As a result of this broad definition, violations of the Wire Act, the Travel Act, the IGBA and other relevant U.S.C. sections, to the extent that they involve gambling punishable by imprisonment for more than one year, also imply a violation of the RICO Act. One should note that the RICO Act provides for both very serious criminal sanctions (fines and/or imprisonment of up to 20 years, in accordance with 18 U.S.C. § 1963) and for civil remedies (including divestitures, restrictions on future activities, threefold damages, costs and attorneys fees, in accordance with 18 U.S.C. § 1964).

C.2.6. State laws

State laws are relevant to this investigation both because of the prohibitions on gambling and betting that they contain, and because in many cases it is the violation of state laws that generates the violation of federal laws.

The question of which states prohibit remote gambling is a complex one, and a detailed analysis of the relevant state laws in order to determine which states (and to what extent) prohibit remote gambling cannot be provided in this report. However, according to information received in the context of the investigation, eight states expressly prohibit Internet gambling.⁷⁵ Other states regard their gambling prohibitions also to extend to Internet-based activities, even where this is not expressly stated in the relevant

⁷⁵ Illinois, Indiana, Louisiana, Montana, Nevada, Oregon, South Dakota and Washington.

legislation. This is also the conclusion of the GAO report,⁷⁶ which, interestingly, also remarks that "federal law is used to protect the states from having their laws circumvented".⁷⁷

The applicability of the relevant prohibitions may also depend on factors subject to interpretation such as whether the relevant gambling is considered to be a game of chance or of skill. Two other factors that are relevant to the applicability of state laws have been discussed in some detail above: first, the location where the prohibited gambling activity takes place (where the consumer is located, or where the gaming company or its servers are located); second, the "dormant commerce clause" doctrine, which limits the ability of states to restrict interstate commerce.

One should note in this respect that the Panel in *US-Gambling* found that Antigua had provided *prima facie* evidence that the laws of Louisiana, Massachusetts, South Dakota and Utah contained gambling prohibitions in violation of Article XVI of the GATS.⁷⁸ This finding was later reversed by the Appellate Body,⁷⁹ who found that Antigua had not sufficiently connected the state laws with Article XVI.

A substantial number of states appear indeed to allow some form of remote or Internet gambling. According to information supplied by Antigua and reflected in the 21.5 Panel Report in *US-Gambling*,⁸⁰ at least 18 states authorize "account wagering". Most of the relevant laws expressly refer to IHA,⁸¹ and to account wagering by telephone, Internet and/or other electronic means. Some even purportedly authorize account wagering on an interstate basis. Some of the state laws apply to wagering not only on horse racing, but to wagering on other sports (greyhound racing, dog racing and/or jai alai) as well. All this information has also been supplied in the context of this investigation, as well as evidence demonstrating "the existence of a flourishing remote account wagering industry on horse racing in the United States operating in ostensible legality."⁸²

As far as Nevada is concerned, a wide variety of "interactive gaming" activities can be offered, which involve the use of "communications technology". However, this is limited to resort hotels that already hold a Nevada gaming license. Moreover, it is also allowed

⁷⁶ See p. 16 of "Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002

⁷⁷ "In general, gambling is a matter of state law, with each state determining whether individuals can gamble within its borders and whether gaming businesses can legally operate there. Since Internet gambling typically occurs through interstate or international means, with a Web site located in one state or country and the gambler in another, federal law is used to protect the states from having their laws circumvented." Internet Gambling: an Overview of the Issues." United States General Accounting Office. Report to Congressional Requesters. December 2002, p. 11. This way of arguing is quite different from the DOJ view that state law cannot overrule a federal prohibition

⁷⁸ Panel Report, *US-Gambling*, para. 6.421

⁷⁹ Appellate Body Report, *US-Gambling*, para.155

⁸⁰ 21.5 Panel Report, *US-Gambling*, para. 6.113

⁸¹ See in this respect Antigua's first written submission, Recourse by Antigua and Barbuda to Article 21.5 of the DSU, *US-Gambling*, para. 67

⁸² In the words of the 21.5 Panel in *US-Gambling*, para. 6.116

for licensed operators to offer "race books or sports pools" using communications technology, as long as this is done under license and only for wagers originating within the state of Nevada for races or sporting events.⁸³

C.2.7. State lotteries

State lotteries are operated by a large majority of US states. Some do not operate lotteries (e.g. Nevada, Utah, or Wyoming) but this is the exception rather than the rule. All the US state lotteries are members of NASPL. According to the NASPL, in the US lottery is not offered by remote supply. There is no remote access to lottery services, be it by the Internet or otherwise. US state licensed lotteries do not have the legal right to solicit or award prizes in interstate commerce using the telephone or the Internet. It is nonetheless possible in some states to purchase a subscription to lotteries that are sold via terminals.

According to NASPL, the lotteries of New Hampshire, North Dakota and New York currently offer some lottery games that can be played via subscriptions purchased via the Internet. This possibility would only be available to players located in the relevant state. However, it appears that subscriptions from the relevant websites appear also to be possible for local residents from Maryland, Vermont and Virginia.⁸⁴

Also, there can be specificities in the gaming services offered by each of the lotteries. As indicated by the New York lottery in the context of this investigation, "the legislation as to what gaming activity is permitted within the state varies from state to state. For example, in New York it has been determined that land based video gaming machines that display the result of an electronic instant game fall within the definition of "instant lotteries" and therefore can be operated by the New York Lottery."

The question of remote lottery gambling was addressed by Antigua in the *US-Gambling* case. As indicated by Antigua in its first submission to the 21.5 Panel, subscriptions are available also on a cross-border basis from the Massachusetts State Lottery.

The remote sales by this lottery are described in the following way on its website:

"Can non-residents play the game? If so, how do they collect?"

Yes, anyone 18 and over can purchase any Lottery product at any agent location. All players can collect their prizes at the same locations listed in question four. Additionally, Season Tickets can be purchased directly from any sales agent while in the state or from out of state, by calling 1-800-222-TKTS. The ticket can be registered in the owner's name by completing and returning the registration form to the Lottery. Season Tickets are available for Megabucks, Mass Cash, Mega Millions and Cash Winfall."⁸⁵

⁸³ Nevada Revised Statutes, 463 and 465.

⁸⁴ While this report was being drafted, the Virginia lottery was updating the relevant section of its website. As a result, the purchase of subscriptions over the Internet was temporarily unavailable.

⁸⁵ <http://www.masslottery.com/about/faq.html>

Antigua offered to the 21.5 Panel further examples of remote purchase of lottery tickets via telephone or mail, such as Illinois (where the lottery may according with state laws also sell its products by means of electronic transmission) or Maine.

C.2.8. *US rules on criminal procedure*

C.2.8.1. Plea agreements

Referring to publicly available information, the complaint explained that the DOJ had launched investigations into the activities of certain non-US Internet gaming companies in the US prior to October 2006. The investigations involved the issuing of *subpoenas* to these companies and also to banks which had provided supporting services to the gaming industry. It further explained that criminal investigations in the US often imply negotiations between the prosecutors and the defendants that can result in a settlement or agreement ("plea agreement" or "plea bargain"), subject to approval by a court. It further provided the example of Neteller, an Internet payment processor that worked for the Internet gaming industry, whose settlement with the DOJ included the payment of a \$126 million fine.⁸⁶

A plea agreement (or plea bargain) is an agreement in a criminal case between the defendant and the prosecutor, by which the defendant accepts the prosecutor's offer to plead guilty to either the charged offense or a lesser related offense. As a result, the defendant avoids trial (with its added cost and publicity) and usually avoids the risk of being convicted of the more serious charges that would be brought against him if he chose to stand trial. The plea bargain is also useful for the prosecuting authority, as it avoids the cost, time and uncertainty of going to trial. The system of plea agreements or plea bargaining is usual in common law systems, but can also be found beyond. A vast majority⁸⁷ of criminal cases in the US are resolved through plea bargains, which in all but exceptional circumstances are endorsed by the courts.

According to views expressed in the context of this investigation, the practice of plea bargaining has indeed become a central feature in the administration of criminal justice in the US, and can often be of benefit to prosecutor, defendant and the legal system as a whole. This will typically happen in cases where the guilt of the defendant is not seriously in doubt. There is, however, a different type of plea bargain situation in which the guilt of the accused may be strongly contested and the evidence in the hands of the prosecutor relatively weak. In such cases, it is argued that the plea bargain provides a powerful and asymmetrical weapon in the hands of the prosecution, as the bargain that the prosecutor will offer will be crafted in such a way as to make it virtually impossible for the defendant to reject. Typically, the defendant will be threatened with a heavy indictment which, if accepted by a jury, could carry a very heavy sentence, unless the

⁸⁶ In addition, two Canadian founders of Neteller separately agreed to forfeit \$ 100 million in July 2007 when they pleaded guilty to charges of conspiracy to transfer funds with the intent to promote illegal gambling.

⁸⁷ "Although, historically, the majority of criminal defendants enter a plea of guilty prior to trial, the United States Attorneys must always be prepared to go to trial." United States' Attorneys Annual Statistical Report, Fiscal Year 2007, US Department of Justice at http://www.usdoj.gov/usao/reading_room/reports/asr2007/07statrpt.pdf. This has generated a debate on whether the pervasive presence of plea bargaining in the system goes against basic constitutional rights. See e.g. "The Case Against Plea Bargaining", Timothy Lynch, Cato Institute, at <http://www.cato.org/pubs/regulation/regv26n3/v26n3-7.pdf>.

defendant pleads guilty to charges carrying a lighter sentence. The advantage to the prosecutor in this second type of cases is that he will be able to secure a conviction even in the face of a weak substantive or evidentiary case.⁸⁸

The concept of plea agreements is recognised and codified in the Federal Rules of Criminal Procedure, Rule 11.⁸⁹ The US Attorney's Manual (USAM) provides further guidance for US attorneys in this matter.⁹⁰ It specifically indicates that plea agreements should honestly reflect the totality and seriousness of the defendant's conduct, and any departure to which the prosecutor is agreeing. The basic alternatives that government attorneys have upon the defendant's plea of guilty (or *nolo contendere*) to a charged offense or to a lesser or related offense, are to dismiss other charges; take a certain position regarding the sentence to be imposed; or combine a plea with a dismissal of charges and an undertaking by the prosecutor concerning the government's position at sentencing.

⁸⁸ In *Bordenkircher v. Hayes*, 434 U.S. 357 (1978), the US Supreme Court held that it was consistent with the US Constitution "when a state prosecutor carries out a threat made during plea negotiations to reindict the accused on more serious charges if he does not plead guilty to the offense with which he was originally charged."

⁸⁹ Federal Rules of Criminal Procedure (December 1, 2007. The Committee on the Judiciary, House of Representatives).

Rule 11. Pleas

"(c) Plea Agreement Procedure.

(1) In General. An attorney for the government and the defendant's attorney, or the defendant when proceeding pro se, may discuss and reach a plea agreement. The court must not participate in these discussions. If the defendant pleads guilty or *nolo contendere* to either a charged offense or a lesser or related offense, the plea agreement may specify that an attorney for the government will:

(A) not bring, or will move to dismiss, other charges;

(B) recommend, or agree not to oppose the defendant's request, that a particular sentence or sentencing range is appropriate or that a particular provision of the Sentencing Guidelines, or policy statement, or sentencing factor does or does not apply (such a recommendation or request does not bind the court); or

(C) agree that a specific sentence or sentencing range is the appropriate disposition of the case, or that a particular provision of the Sentencing Guidelines, or policy statement, or sentencing factor does or does not apply (such a recommendation or request binds the court once the court accepts the plea agreement).

(2) Disclosing a Plea Agreement. The parties must disclose the plea agreement in open court when the plea is offered, unless the court for good cause allows the parties to disclose the plea agreement in camera.

(3) Judicial Consideration of a Plea Agreement.

(A) To the extent the plea agreement is of the type specified in Rule 11(c)(1)(A) or (C), the court may accept the agreement, reject it, or defer a decision until the court has reviewed the presentence report.

(B) To the extent the plea agreement is of the type specified in Rule 11(c)(1)(B), the court must advise the defendant that the defendant has no right to withdraw the plea if the court does not follow the recommendation or request."

⁹⁰ See USAM 9 – 16.300, 9 – 27.400 et seq.

The USAM also indicates in 9-27.420 that attorneys should weigh all relevant considerations in determining whether it would be appropriate to enter in a plea agreement. Such considerations include for example the defendant's willingness to cooperate in the investigation or prosecution of others, the nature and seriousness of the offenses charged, the desirability of prompt and certain disposition of the case or the likelihood of obtaining a conviction at trial. On the question of the likelihood of conviction, the USAM comments to 9-27.420 indicate that "the prosecutor should weigh the strength of the government's case relative to the anticipated defense case, bearing in mind legal and evidentiary problems that might be expected..." but also that "it obviously is improper for the prosecutor to attempt to dispose of a case by means of a plea agreement if he/she is not satisfied that the legal standards for guilt are met."

C.2.8.2. Initiating and declining charges – impermissible considerations in accordance with the USAM

National origin appears to be an impermissible consideration for US Attorneys when initiating or declining charges. In effect, according to USAM 9-27.260, in determining whether to commence or recommend prosecution or take other action against a person, the attorney for the government should not be influenced by:

1. The person's race, religion, sex, *national origin*, or political association, activities or beliefs;
2. The attorney's own personal feelings concerning the person, the person's associates, or the victim; or
3. The possible affect of the decision on the attorney's own professional or personal circumstances." (emphasis added)

C.3. The challenged measures: enforcement activities

According to the complaint, the US is enforcing its gambling laws in a discriminatory way. While EU operators of Internet gambling have been forced to stop offering gambling services to persons in the US, US operators of certain types of Internet gambling are allowed to operate. Furthermore, it is argued that EU operators are threatened with severe criminal sanctions, even though they have ceased their US activities, while US operators in a similar legal position are allowed to continue their operations.

A proper analysis of enforcement cases obviously requires to look not only at enforcement actions launched against EU suppliers, but also at enforcement actions (or lack thereof) against US suppliers. This is particularly relevant given the view of the US government expressed in the context of this investigation that there is no basis for any allegation of "discriminatory enforcement" of US gambling laws, and that nationality of the defendant is not a factor in any enforcement-related decision making. As specifically noted by the US government, quoting the Appellate Body in *US-Gambling*, "enforcement agencies may refrain from prosecution in many instances for reasons unrelated to discriminatory intent and without discriminatory effect."⁹¹

⁹¹ Appellate Body Report, *US-Gambling*, para. 356

It is important to note that according to information provided by the US government in this investigation, although the DOJ publishes summary statistics in the *Compendium of Federal Justice Statistics*,⁹² the statistics do not break down prosecutions based on the nationality of the defendant. Depending on the specifics of the individual case, the *Compendium* will most often categorize gambling prosecutions as "gambling" or "racketeering", but may also include them in other categories such as "tax violations" or "conspiracy". In fiscal year 2004, the DOJ prosecuted over 1,800 persons for gambling and racketeering offenses.

C.3.1. Enforcement relating to EU suppliers

There has been substantial enforcement activity by the DOJ against EU Internet gambling and betting companies and their shareholders and executives. This activity includes cases where the investigation has resulted in formal charges being brought against EU companies and executives and/or a settlement with the authorities, and cases where a criminal investigation has been launched and is ongoing but has not yet resulted in formal charges being brought.

Information in this respect submitted to the Commission services in the context of this investigation includes the following cases:

- **Betonsports:** an indictment invoking several federal and state laws was issued in July 2006 against Betonsports Plc, as well as against a number of individuals including Gary Kaplan, its founder, and David Carruthers, its former chief executive. David Carruthers and Gary Kaplan were arrested in July 2006 and March 2007 respectively. Betonsports pleaded guilty in May 2007 to racketeering and conspiracy charges and no longer operates. The cases against the indicted individuals are still pending.
- **SportingBet:** Peter Dicks, non-executive chairman of Sportingbet Plc, was arrested in September 2006 in New York. His extradition warrant was finally dismissed, and the company settled the charges with the Louisiana parish that had issued the arrest warrant. Sportingbet has been reported to be in ongoing discussions with the DOJ.
- **Partygaming:** Partygaming Plc announced in June 2007 that it had initiated discussions with the DOJ (United States Attorney's Office for the Southern District of New York) in the context of an investigation on specific gambling and betting companies. The investigation is still ongoing. According to an announcement by Partygaming on 16 December 2008, the discussions with the DOJ have made good progress and the company is negotiating the final terms of a possible settlement. In parallel, and following an investigation by the same Attorney's Office, Partygaming founder and shareholder Anurag Dikshit pleaded guilty on 16 December 2008 to charges under the Wire Act and faces a maximum sentence of 2 years in prison and a substantial fine. Moreover, Mr Dikshit agreed to forfeit \$300 million, of which he has already paid the first \$100 million. Sentencing is scheduled for 16 December 2010, until which time Mr Dikshit will have to co-operate with DOJ investigations. Mr Dikshit is a national of India.

⁹² Available at <http://www.ojp.usdoj.gov/bjs/abstract/cfjs04.htm> for fiscal year 2004 (most recent year available)

- 888: 888 Holdings Plc announced in June 2007 that it had initiated discussions with the DOJ (United States Attorney's Office for the Southern District of New York) in the context of an investigation on specific gambling and betting companies. The investigation is still ongoing.

The Commission services have knowledge of several other EU companies that have provided Internet (sports and non-sports) gambling and betting services to customers located in the US, and that are referenced in section B.2 above. Irrespective of the specific enforcement actions that may currently be ongoing with respect to EU suppliers, it is not excluded that enforcement actions could be launched in the future with respect to remote gambling and betting services offered in the past by EU companies to US customers.

DOJ enforcement activity has also targeted suppliers of supporting services to EU gambling and betting companies that had been operating in the US. The Commission services are aware of the following cases:

- Neteller: Neteller Plc is a payment processor headquartered in the Isle of Man⁹³ listed on the Alternative Investment Market of the London Stock Exchange (now as NEOVIA Financial Plc) and regulated by the UK Financial Services Authority, with a focus on online gambling-related transactions. It announced on 18 July 2007 that it had entered into a plea agreement with the DOJ (United States Attorney's Office for the Southern District of New York) which included the admission of criminal conduct and the forfeiture of \$136 million. The two founders of Neteller, Stephen Lawrence and John Lefevbre, both Canadian citizens, were arrested in January 2007 and pleaded in July 2007 guilty to conspiracy to promote illegal Internet gambling, agreeing also to forfeit \$100 million.
- FireOne: FireOne Group Plc is a payment processor based in Ireland whose Canadian parent company Optimal Group announced in May 2007 that it was in discussions with the DOJ (United States Attorney's Office for the Southern District of New York) in relation to the ongoing investigations on online gambling companies and that the DOJ had seized around \$20 million of its funds.
- Banks: according to press reports of 2007, several international banks, including HSBC, Dresdner Kleinwort, Deutsche Bank and Credit Suisse, received *sub poenas* issued by the DOJ requesting information in connection with their provision of services to EU Internet gambling operators, including the underwriting of initial public offerings, share brokerage and the provision of advice.

The Commission services have knowledge of specific concerns of suppliers of supporting services to EU gambling and betting companies, including suppliers not specifically mentioned in this report, with DOJ enforcement actions. Irrespective of specific enforcement actions that may currently be ongoing with respect to specific EU suppliers of supporting services to EU gambling and betting companies, it is not

⁹³ The Isle of Man is not part of the EU. However, Neteller (UK) Limited is a wholly-owned subsidiary of NEOVIA Financial Plc which is authorised and regulated by the Financial Services Authority (FSA) as an e-money issuer. It operates across the EU on the basis of this authorisation. NEOVIA Financial Plc is listed on the London Stock Exchange's AIM market (ticker: NEO), having achieved its listing as Neteller Plc (ticker: NLR) in April 2004. Neteller Plc changed its name to NEOVIA Financial Plc on 17 November 2008.

excluded that enforcement actions could be launched in the future in connection with remote gambling and betting services offered in the past by EU companies to US customers.

C.3.2. Enforcement relating to US suppliers

In the context of this investigation, the Commission services have received information about enforcement cases – ongoing or completed, at state or federal level - involving US nationals and/or suppliers, including the following:

- Gold Medal Sports: Gold Medal Sports was an offshore sportsbook located on the island of Curacao owned by US citizens. It operated via phone lines and the Internet. The company pleaded guilty to racketeering in December 2001, and agreed to suspend operations and forfeit \$3.3 million. Several US individuals involved in this case were also prosecuted on charges including conspiracy and aiding and abetting in violations of the Wire Act.
- Lombardo: Baron Lombardo and six other individuals of Las Vegas as well as four companies, including two US companies, were prosecuted for assisting Internet gambling companies by providing the means to process payments.
- Cohen: Jay Cohen was co-founder and president of World Sports Exchange, an Antigua-based company engaged in bookmaking on US sporting events. He was arrested in 1998 and convicted to 21 months imprisonment and a fine in 2001.
- Bet the Duck: Bettheduck.com was an offshore sportsbook operation with a call centre in Costa Rica. Charges were brought in connection with the operation of this business and the receipt of bets and wagers through both the internet and a toll-free phone number and activities by some of the defendants as agents, collecting bets and wagers from players and delivering payments to D. L. Duckart, who ran the business. Some defendants pleaded guilty to certain charges brought under federal laws (Travel Act, IGBA, legislation on money laundering). D. L. Duckhart pleaded guilty and was sentenced to eight months' imprisonment, fine and forfeiture. The case against some of the defendants is still pending.
- Worldwide Telesports: in May 2006, Worldwide Telesports Inc., its owner W. Scott and employee J. Davis were indicted for offences relating to Internet gambling. WWTS was located in Antigua and operated through various jurisdictions with the purpose of offering Internet gambling services to US customers. W. Scott is reported to have renounced his US citizenship and moved out of the US in 2004.
- Gianelli: as part of a larger case, charges were brought in relation to the operation of an offshore Internet gambling site (www.dukesportweb.com) based on violations of the Wire Act in relation to sports betting activities. The Travel Act is also mentioned in this case.
- Cicalese: twelve persons, including C. Cicalese, were indicted in 2007 as a result of their engagement in the operations of the so-called "Cicalese Wireroom", based in Antigua but supplying the US via telephone and some websites, and operating on the basis of persons based in the US who acted as intermediaries ("runners" and "bookies") between the wireroom and the gamblers.

- Paradise Casino: Hoss Limited, Inc., a company incorporated in Nevada and doing business as Paradise Casino, and its two owners, Marc Meghrouni and Scott Shaver, pleaded guilty in 2006 to charges under the Wire Act and US legislation against money laundering and on taxation. Paradise Casino had operated an offshore sportsbook originally in Antigua, and then in Curaçao in the Netherlands Antilles targeted at US customers using telephone and computer communications.
- World Interactive Gaming: The World Interactive Gambling Corporation was a Delaware corporation headquartered in New York which controlled the services offered by its subsidiary Golden Chips Casino, Inc., incorporated in Antigua. The services offered consisted of non-sports gambling via an Internet casino. The World Interactive Gambling Corporation was found to violate New York criminal laws, and also the Wire Act, the travel Act and the ITWA.
- Interactive Gaming and Communications: Interactive Gaming & Communications Corp. was a Delaware corporation with its principal place of business in Pennsylvania. It operated a website directing those interested in gaming activities towards the services offered by its subsidiary Global Casino Ltd., a Grenada corporation, which a Missouri Circuit Court found in violation of Missouri's laws in 1997.
- World Wide Wagering: the investigation into the Internet sportsbook gambling services offered by the World Wide Wagering Inc. located offshore in Dominica, led to the conviction of seven US nationals, including H. Meyers of Rockville, Maryland, involved in the offering Internet gambling services between 2003 and 2004.
- Playwithal: in 2006, 27 individuals and three companies located in the US which had provided services to an offshore remote gambling company (Costa Rica-based "Playwithal Sportsbook"), were indicted for their role in the setting up and operation of this online gambling enterprise. These three companies were Primary Development, Inc., based in New York; Prolexic Technologies, Inc., based in Florida; and D.S. Networks, S.A., Inc., based in Florida. The defendants were all considered part of the "Playwithal Gambling Organization" which operated an unlawful gambling enterprise in Queens County and elsewhere. At least two individuals have already been sentenced.
- Case involving Westchester, The Bronx, Manhattan in New York, and Somerset and Essex in New Jersey: 18 individuals were arrested in New York and New Jersey in 2007 as a result of an investigation on sports betting and gambling involving the use of around 60 websites (such as betoss.com or pacificsportsbooks.com) and a wire room located offshore in Costa Rica.
- Youbet.com: the situation of Youbet.com had been subject to analysis in the *US-Gambling* case as a result of a disclosure in its annual 2002 report that it faced the risk of criminal proceedings and penalties.⁹⁴ It has been reported that the US Attorney's Office in Nevada had been investigating the activities of International Racing Group (IRG) customers and a former owner of IRG, and had seized IRG funds amounting to

⁹⁴ Panel Report, *US-Gambling*, para. 6.587. See also Article 21.5 Panel report, paras. 6.82 and 6.107, according to which the DOJ was not aware of "any public pending prosecution of the suppliers in the US mentioned in the original proceeding"

\$1.5 million. IRG was a Youbet.com subsidiary that Youbet.com acquired in 2005 originally based off-shore, which Youbet subsequently moved to Oregon in 2005. As a result of the investigation, Youbet.com closed IRG in February 2008. In March 2008, Youbet.com announced the terms of an agreement signed with the US Attorney's Office in Las Vegas, according to which the government agreed not to pursue any charges against Youbet or its subsidiaries. In exchange, the company agreed to continue cooperating with the government in its investigation.⁹⁵

- Sporting News: The Sporting News (Vulcan Sports Media, Inc.), incorporated in Missouri, was investigated for having promoted illegal gambling by accepting fees in exchange of advertising internet and telephonic gambling enterprises to its US print, internet and radio media audiences. This investigation was settled via a \$7.2 million agreement with the DOJ in 2006.
- Citibank: as a result of an investigation launched by the Attorney General of the State of New York, Citibank agreed in 2002 to block online gambling transactions through MasterCard and Visa credit cards issued by the bank, and to pay \$100,000 in costs to the State of New York, in addition to providing \$400,000 to not-for-profit organisations addressing gambling. This settlement triggered further agreements with 10 other banks in February 2003, which also agreed to block online gambling transactions and to pay \$335,000 in costs to the State of New York.
- PayPal: in July 2003, PayPal, and its parent eBay, entered into a civil settlement agreement with the United States Attorney's Office for the Eastern District of Missouri to settle allegations it aided in illegal offshore and on-line gambling activities. As part of the agreement, PayPal agreed to forfeit \$10 million, representing proceeds derived by PayPal from the processing of illegal gambling transactions.
- ECHO: a non-prosecution agreement between Electronic Clearing House, Inc (ECHO) was announced in March 2007 by the United States Attorney's Office for the Southern District of New York. ECHO had been involved in the transfer of money on behalf of various online payment services companies, known as "e-wallets." The agreement implied further cooperation of ECHO with the US Government's investigation into Internet gambling, and the payment of \$2.3 million, which was the equivalent of the net proceeds from the services that ECHO had provided to e-wallets since 2001. The United States Attorney's Office for the Southern District of New York observed that criminal prosecution would in this case not serve the public interest, and referred to the factors set forth in the DOJ "Principles of Federal Prosecution of Business Organizations" to justify its decision.
- Microsoft, Google and Yahoo: in December 2007, Microsoft Corporation, Google and Yahoo! agreed to pay a total of \$31.5 million to resolve claims that between 1997 and

⁹⁵ The US Attorney's Office in Nevada has not published any information regarding this investigation. However, it appears that the investigation was linked to IRG's off-shore operations. Therefore, although this implies that a supplier of online racing and betting services on horse racing has been subject to enforcement actions, this enforcement action would relate to the specific fact of the existence of off-shore operations, and not to the fact that Youbet.com offers online gambling and betting services. Youbet.com continues to operate its online gambling and betting business. As a result, this enforcement action against Youbet.com would actually support the interpretation that there is no US enforcement against the online supply of remote gambling and betting services on horse racing, and that enforcement only targets the cross-border (remote) supply of gambling and betting services.

2007 they received payments from online gambling businesses for advertising online gambling. None of the companies admitted or contested that they had received payments from online gambling businesses for advertising, although their conduct had been considered to violate the Wire Act, wagering excise tax laws and various state and municipal laws prohibiting gambling.

The Commission services have also received information concerning suppliers offering remote gambling and betting services on horse racing and dog racing. The information provided follows closely the evidence submitted by Antigua in the Article 21.5 DSU proceedings in *US-Gambling*. In accordance with the relevant evidence submitted in those proceedings by Antigua, there were over 20 domestic operators of remote gambling and betting services with licenses issued by one or more states, including companies with shares listed on major stock exchanges and companies owned by states or other governmental bodies. The relevant evidence was summarised by the Article 21.5 Panel in *US-Gambling* in the following way:

"The suppliers in relation to which Antigua submits evidence in the compliance proceeding hold licences granted by State governments under the State laws and regulations referred to in paragraph 6.113 above to conduct remote account wagering, or are public benefit corporations established for this purpose. Some of these licences are expressly limited to remote wagering in the State "that is permissible under the Interstate Horseracing Act". Some of the suppliers and industry associations also confirm that they operate under the IHA. Most of these suppliers state that they accept wagers placed in other States. These suppliers are substantial and even prominent businesses with, collectively, thousands of employees and apparently tens of thousands of clients, paying taxes or generating revenue for government owners, having traded openly for up to 30 years and in some cases even operating television channels. Three are publicly listed corporations making filings with the United States Securities and Exchange Commission or subsidiaries of such corporations."⁹⁶

The information regarding specific suppliers of this type obtained by the Commission in the context of this investigation can be summarised as follows:

- YouBet.com, Inc. ("YouBet") is a leading United States-based provider of telephone and Internet account wagering services on horse races which has processed over \$2.5 billion in wagers from 1 January 2002 to 31 December 2007. YouBet has licenses in the states of California, Idaho, Oregon and Washington and accepts pari-mutuel wagers from punters in other states, including states where existing state laws purport to prohibit or restrict the ability to accept pari-mutuel wagers from such states. Total wagers placed in 2007 amounted to \$716.0 million.
- XpressBet, Inc. ("XpressBet") is a remote account wagering operator with offices located in eight states in the United States. XpressBet is a wholly-owned subsidiary of Magna Entertainment Corp., a publicly held company ("MEC"), and permits customers from 39 states to place wagers by telephone and over the Internet on horse races at over 100 North American racetracks and internationally on races in Australia, South Africa and Dubai. For the year 2007, the amount wagered through XpressBet

⁹⁶ Article 21.5 Panel Report, *US-Gambling*, para. 6.115 (footnotes omitted)

was approximately \$175.6 million. In addition to XpressBet, MEC owns and operates Horse Racing TV, a 24-hour horse racing television network, and operates a Europe-facing Internet site offering betting on horse races from the United States and elsewhere to consumers in a number of European countries.

- TVG is an advance deposit wagering service and is wholly-owned and operated by Gemstar-TV Guide International, Inc. On 6 December 2007, Gemstar agreed to be acquired by Macrovision Corporation. TVG offers a remote wagering service that “combines live, televised coverage from over 60 of America’s premier tracks with the convenience of wagering from home online, by phone, and where available, set-top remote control.” TVG accepts Internet, telephone and satellite television account wagering from residents of 12 states. Players can open accounts on the Internet, by telephone or through the post, and can fund accounts by check, money order, credit card or debit card. In the year 2007, TVG processed \$477.9 million in wagers. TVG is licensed by the Oregon Racing Commission, California Horse Racing Board and the Washington Horse Racing Commission.
- The Racing Channel, Inc. (the “Racing Channel”) is an Internet-based pari-mutuel account wagering service licensed by the State of Oregon. It is a wholly-owned subsidiary of Greenwood Racing, Inc. (“GRI”), a leader in pari-mutuel wagering through its racetrack, off-track and account wagering operations. GRI produces live racing coverage that is distributed on the Racing Television Network via cable and satellite broadcasting. In 2004, the Racing Channel changed to a free subscriber based system open to active account holders of Oneclickbetting.com, Phonebet.com, Colonialdowns.com and CDPhonebet.com. All Racing Channel account wagering is “hubbed” through its service in Oregon. The Racing Channel takes wagers from residents of 33 US states and six territories, and processed wagers aggregating \$99.8 million in 2005.
- Churchill Downs Inc. operates the "Twin Spires" remote gambling service. Churchill Downs Inc. has recently also acquired WinTicket.com, BrisBet.com, TsnBet.com and AmericaTAB. AmericaTab is licensed by the Oregon Racing Commission, and, in 2005, processed bets aggregating USD \$126.7 million. AmericaTab accepts accounts from residents of 35 US states.
- US Off Track, LLC (“US Off-Track”) is another account wagering service that owns and operates PayDog.com, an Internet site offering racing and wagering for the greyhound, thoroughbred and harness industry. US Off-Track is licensed by the Oregon Racing Commission. US Off-Track’s “PayDog” product offers teller-assisted telephone, touch-tone and voice recognition wagering. Users may also place a wager online from a home computer or from a wireless Internet ready phone or Palm device. Customers from 35 states may fund accounts by online deposits through credit or debit card, wire transfer and other conventional means. US Off-Track reported total wagers of \$25.8 million for 2005.
- Capital District Regional Off-Track Betting Corporation (“Capital OTB”) is a public benefit corporation owned and operated by the State of New York that offers account wagering on horse races via the telephone and the Internet. Capital OTB also owns and operates its own horse racing television station that allows patrons to wager through Capital OTB’s account wagering system “from the comforts of home.” There are no apparent restrictions on locations that punters may wager from, “enabling

customers to wager from almost anywhere in the world.” According to the company, Capital OTB processes bets aggregating more than \$200 million annually.

- The New York City Off-Track Betting Corporation (“NYCOTB”) is a remote account wagering operator owned by the city of New York. NYCOTB was established in 1971 as the first legal, offtrack, pari-mutuel wagering operation in the US. NYCOTB processes over \$1.0 billion in wagers annually, and with more than 40,000 phone accounts, NYCOTB is the largest telephone betting operation in the US. NYCOTB also has its own official internet wagering site. The only restrictions set out on its website are that wagering is not available to residents of states where account wagering is prohibited and that account holders who are residents of California, Florida and Kansas cannot wager on tracks in their applicable home state and that New Jersey residents cannot wager through their NYCOTB account when physically wagering from New Jersey.
- New Jersey Account Wagering (“NJAW”) is owned by a public corporation of the state of New Jersey and offers account wagering on horse racing to New Jersey residents only, by telephone and the Internet. A single NJAW account can be used to bet online, by telephone and at self-service terminals or hand-held devices located throughout New Jersey racetracks.

These descriptions are enough to demonstrate that these companies operate in the US "in ostensible legality", as the Article 21.5 Panel in *US-Gambling* put it.⁹⁷ There is no evidence of any DOJ enforcement action against any of these companies.

The inactivity of the DOJ with respect to these companies – which has been confirmed in this investigation – led the Article 21.5 Panel in *US-Gambling* to observe that "[I]t is striking that the Department of Justice had not, apparently, ever initiated a criminal prosecution under the measures at issue of a pari-mutuel wagering supplier in the United States who transmit bets and wagers in violation of the Wire Act but who, at the same time, has obtained consent from the horse racing associations and shares its revenue with the racetracks in accordance with the IHA."⁹⁸ The continued absence of enforcement activity against US suppliers of online pari-mutuel wagering on horse racing is also coherent with the situation described by the Article 21.5 Panel in *US-Gambling*.⁹⁹

In sum, the lack of enforcement action by the DOJ against this type of suppliers appears to vindicate the well-known position of US suppliers of online gambling on horse racing that this type of remote gambling is, indeed, allowed in the US. This position was expressed once again by the National Thoroughbred Racing Association in a press release on 30 September 2006 after the passage of the UIGEA, in the following way:

"The legislation contained language that recognizes the ability of the horse racing industry to offer account wagering under the IHA of 1978 as amended. These important protections were also contained in the House-passed bill and are similar to other provisions introduced over the last few years....Passage of

⁹⁷ Article 21.5 Panel Report, *US-Gambling*, para. 6.116

⁹⁸ Article 21.5 Panel Report, *US-Gambling*, para. 6.126

⁹⁹ Article 21.5 Panel Report, *US-Gambling*, para. 6.128

this legislation is a major victory for the horse racing and breeding industry and culminates an eight-year effort to protect the industry's right to conduct state licensed and regulated account wagering, the fastest growing segment of pari-mutuel wagering."¹⁰⁰

C.3.3. *Conclusion on enforcement*

In conclusion, there is evidence of enforcement of US gambling legislation both against EU and US suppliers of online gambling services. Although there are some indications that the prosecution of certain comparable cases has resulted in more lenient treatment of US suppliers, these indications are not sufficient to conclude that EU suppliers are being discriminated against specifically on the basis of their nationality.

However, the information available to the Commission services does support the conclusion that - at least - suppliers of online gambling services on horse racing (and dog racing) are not subject to enforcement in the form of criminal prosecution in the US. As a result, the Commission services consider that the allegation in the complaint that US operators of certain types of Internet gambling are allowed to operate in the US is fully justified.

C.4. **Legal analysis**

C.4.1. *Measures*

C.4.1.1. Introduction

The complaint describes its scope as covering (i) US legislation imposing a ban on internet gambling; (ii) measures taken to enforce that legislation; (iii) the fact that the legislation is enforced in a discriminatory way.

In this respect, the complaint explicitly identified the relevant provisions in the US Wire Act and the safe harbour allegedly created by the Interstate Horse Racing Act; the Travel Act; the Illegal Gambling Business Act; the Wagering Paraphernalia Act, and Federal anti-money laundering legislation; prohibitions contained in State laws; the Unlawful Internet Gambling Enforcement Act; and the differential and discriminatory treatment of EU suppliers compared to US suppliers based on these laws.

It further observed that in *US-Gambling*, the debate in its different phases had been obfuscated by a complex discussion about the precise meaning and interpretation of the US laws at issue. Given the unclear domestic legal background, it was often difficult to make a clear distinction between the law, interpretation of the law, and application of the law. In order to avoid the need to conduct such a complex debate, the complaint stated that its choice was to focus on the US authorities' own interpretation of the relevant laws. This interpretation can be summarised through the statement that "[T]he Department of Justice believes that current federal law, including 18 U.S.C. §§ 1084, 1952, and 1955, prohibits all types of gambling over the Internet."¹⁰¹

¹⁰⁰ National Thoroughbred Racing Association, press release 30 September 2006 "Congress Affirms Horse Racing's Position in Internet Gaming; Legislation Passed by both Houses Early this Morning"

¹⁰¹ Letter from William E. Moschella, Assistant Attorney General, to Rep. John Conyers Jr., 13 July 2003

The complainant filed on 24 October 2008 an "Additional Submission on Measures at Issue and Discrimination". This submission provided factual information on the second and third aspects of the complaint (enforcement and discrimination), and also further factual information and legal reasoning relating to the description of the measures at issue in this case and to the alleged GATS violations. It specifically discussed how the US enforcement actions could be qualified as "measures" for the purpose of WTO dispute settlement as "laws as applied"; as individual enforcement actions; and as an enforcement practice.

C.4.1.2. "Measures" in the WTO

A number of WTO provisions¹⁰² appear as relevant when discussing which measures could be challenged in a GATS case. Substantial attention was devoted to this question in the *US-Gambling* case, in particular in order to clarify whether a "total prohibition" that was the "collective effect" of various US laws would qualify as a "measure" that could be challenged in and of itself.

The wording of Article I:1 GATS ("This Agreement applies to measures by Members affecting trade in services") gives the GATS a broad scope of application. As stated by the Appellate Body in this respect in *EC-Bananas III*,¹⁰³ "[I]n our view, the use of the term 'affecting' reflects the intent of the drafters to give a broad reach to the GATS. The ordinary meaning of the word 'affecting' implies a measure that has 'an effect on', which indicates a broad scope of application." This broad scope of application is confirmed by the definitions in Article XXVIII of the GATS, which e.g. defines "measures" as "any measure by a Member, whether in the form of a law, regulation, rule, procedure, decision, administrative action, or any other form."

When considering the question of whether a "total prohibition" constituted a measure that might be challenged under the GATS, the Appellate Body in *US-Gambling* quoted its report in *US – Corrosion-Resistant Steel Sunset Review* and said that, with regard to Article 3.3 of the DSU, "a 'nexus' must exist between the responding Member and the 'measure', such that the 'measure' – whether an act or omission – must be 'attributable' to that Member. Secondly, the 'measure' must be the source of the alleged impairment, which is in turn the effect resulting from the existence or operation of the 'measure'."¹⁰⁴ Moreover, the Appellate Body added that "we note that this distinction between measures and their effects is also evident in the scope of application of the GATS"¹⁰⁵ and that "to the extent that a Member's complaint centres on the effects of an action taken by another Member, that complain must be brought as a challenge to the measure that is the source of the alleged effects."¹⁰⁶

In order for a challenge against measures by a Member to be made, the GATS and the DSU require that a Member specifically identify the measures that are the basis for its

¹⁰² See Panel Report, *US-Gambling*, paras. 6.141 – 6.147

¹⁰³ Appellate Body Report, *EC-Bananas III*

¹⁰⁴ Appellate Body Report, *US-Gambling*, para. 121

¹⁰⁵ *Ibid.*, para. 122

¹⁰⁶ *Ibid.*, para. 123

claims. In particular, Article 6.2 of the DSU requires that Members identify the specific measures at issue in their panel requests. The measure at stake is also important in the implementation phase, given that under Article 19.1 of the DSU, "[W]here a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned bring the measure into conformity with that agreement." As noted by the Appellate Body in *US-Gambling*, being precise as to the specific source of a violation is also justified by the need for the responding party to be able to prepare adequately its defence.¹⁰⁷

Members may challenge legislation as such, independently from the application of that legislation to specific instances.¹⁰⁸ This type of challenge may be supported through examples of the application of that legislation (e.g. on the consistent application of such laws, the pronouncements of domestic courts, etc) as evidence of how the challenged legislation is interpreted and applied.¹⁰⁹ They can also challenge the application of otherwise WTO-consistent legislation whenever they consider that such application is inconsistent with WTO rules. As indicated by the Appellate Body in *US-Corrosion Resistant Steel Sunset Review*, "[I]n principle, any act or omission attributable to a WTO Member can be a measure of that Member for purposes of dispute settlement proceedings."¹¹⁰ In any event, making a *prima facie* case will require the complaining party to put forward evidence and legal argument, knowing that the nature and scope of evidence required in each case will necessarily vary from measure to measure, provision to provision, and case to case.¹¹¹

A question that was raised in the *US-Gambling* case was whether a practice could be considered as an autonomous measure that could be challenged in and of itself. Although the Panel observed that this was the case, the Appellate Body clarified that its jurisprudence had not, to that date, pronounced on this matter.¹¹²

C.4.1.3. The "measures at issue" for the purpose of this examination

The Panel in the *US-Gambling* case did not accept that the US "total prohibition" on the cross-border supply of gambling services could be considered as a "measure" that could be challenged in and of itself. This was explained in the Panel finding, upheld by the Appellate Body, that "the alleged "total prohibition" on the cross-border supply of gambling and betting services describes the alleged effect of an imprecisely defined list of legislative provisions and other instruments and cannot constitute a single and autonomous "measure" than can be challenged in and of itself".¹¹³ Following some

¹⁰⁷ Ibid, para. 125

¹⁰⁸ Appellate Body Report, *US-Corrosion- Resistant Steel Sunset Review*, para. 61

¹⁰⁹ Appellate Body Report, *US-Carbon Steel*, para.157

¹¹⁰ Appellate Body Report, *US-Corrosion Resistant Steel Sunset Review*, para 81

¹¹¹ Appellate Body Report, *US-Gambling*, para. 140 (quoting the Appellate Body reports *Japan-Apples* and *US-Wool Shirts and Blouses*)

¹¹² Appellate Body Report, *US-Gambling*, para. 132

¹¹³ Quoted in Appellate Body Report, *US-Gambling*, para. 126

further analysis of the issue, the Panel concluded that Antigua had challenged specific applications, practices in respect of foreign supply and also the laws at issue.¹¹⁴

In this report, there is a need to "precisely define" which "measures" could be brought before the WTO. The "total prohibition" being excluded as such, a possible challenge could target the following measures:

- The US laws "as such", both at the federal and state level, which prohibit the cross-border supply of gambling and betting services into the US. It is firmly established in WTO jurisprudence that laws can be challenged "as such".¹¹⁵ "As such" cases help in particular "the purpose of preventing future disputes by allowing the root of WTO-inconsistent behaviour to be eliminated."¹¹⁶ This type of challenge would include both the measures that establish the basic prohibition (e.g. the Wire Act), but also those that establish criminal sanctions against the supply of remote gambling services (e.g. the RICO Act). The reason is that these other laws, even where they do not "define" the type of gambling services that are unlawful, do provide for specific criminal sanctions and therefore contribute to the effect of prohibiting the cross-border supply of gambling and betting services. These laws would also include allegedly "permissive" laws, such as the IHA, to the extent that they do not apply to cross-border supply but only to intra- or interstate commerce. The application of the relevant laws by the DOJ through its ongoing enforcement actions could be presented as evidence of the existence of a prohibition.
- The US laws "as applied" by US authorities in respect of gambling and betting services offered by EU companies until their withdrawal from the market in 2006. Indeed, WTO Members may challenge both other Member's laws "as such", and also "any specific application of those laws".¹¹⁷ As a result, and according to WTO jurisprudence, a law may be WTO-inconsistent both "as such" and "as applied", but it may also "as such" and on its face, be consistent with WTO rules and obligations, while at the same time be WTO-inconsistent in its application.¹¹⁸
- Ongoing enforcement actions by the DOJ could be challenged as a discriminatory "practice", in and of itself. The Panel in *US-Gambling* stated, quoting the Panel in *US-Corrosion Resistant Steel Sunset Review*, "that "practice" under WTO law is "a repeated pattern of similar responses to a set of circumstances"". ¹¹⁹ The fact that the Appellate Body has not so far pronounced on the matter of whether a "practice" can be considered as an autonomous measure does not rule out the possibility that a practice could be challenged as such. Obviously, making such a claim would require a solid foundation in the form of sufficient evidence of consistently discriminatory

¹¹⁴ Panel Report, *US-Gambling*, para. 6.190

¹¹⁵ See e.g. Appellate Body Report, *Antidumping Act of 1916*, para. 61; Appellate Body Report, *US-Carbon Steel*, para. 156; Appellate Body Report, *US-Corrosion Resistant Steel Sunset Review*, para. 82.

¹¹⁶ Appellate Body Report, *US-Corrosion Resistant Steel Sunset Review*, para. 82.

¹¹⁷ Appellate Body Report, *US-Carbon Steel*, para. 156

¹¹⁸ Appellate Body Report, *US-Hot-Rolled Steel*, para. 240

¹¹⁹ Panel Report, *US-Gambling*, para. 6.196

application of the prohibition by the DOJ. One should note that the relevant instances of enforcement would need to be placed in their context, including evidence on the overall number of suppliers, enforcement patterns or reasons for particular instances of non-enforcement.¹²⁰

- Individual enforcement actions by the DOJ against EC suppliers could be, in principle, challenged in and of themselves as well, as "separate, autonomous measures". This is supported by the broad scope of the GATS and DSU provisions referred to above, and also by past experience in WTO dispute settlement. The Panel in *US-Gambling* weighed this option in respect of some examples of court cases and other law enforcement actions that were presented by Antigua. However, having listened to Antigua, it finally chose not to consider these individual enforcement actions as separate, autonomous measures, but rather as evidence of the existence of a prohibition on the cross-border supply of gambling and betting services.¹²¹ Also, it is worth recalling in this respect that the claims brought by Australia in *EC-Geographical Indications* included both the relevant law, as such, and the individual registrations effected under the law. However, the panel concluded that Australia had failed to make a *prima facie* case in support of its claims with respect to individual registrations.¹²²

A related question is the definition of what would constitute "enforcement actions" by the DOJ. One could argue that only the formal indictments (or lack thereof) by the DOJ should be considered as relevant "enforcement actions". However, and given the extent of the practice of "plea bargaining" in the US, such an approach would leave a significant part of US criminal enforcement out of WTO dispute settlement scrutiny. This would not be justified. Moreover, WTO dispute settlement jurisprudence clearly suggests that acts or omissions of the organs of the state, notably "executive actions", are covered and can be challenged "as such".¹²³ One should not forget that even non-binding administrative guidance can amount to a governmental measure.¹²⁴ In this particular case, the threat of formal indictments by the DOJ is in many cases more than enough for defendants to plead guilty to the relevant charges. It is therefore clear that the opening of an investigation by the DOJ modifies the "incentives and disincentives" relevant to the

¹²⁰ Appellate Body Report, *US-Gambling*, para. 356

¹²¹ Panel Report, *US-Gambling*, para. 6.195

¹²² Panel Report, *EC-Geographical Indications*, para. 7.751

¹²³ Appellate Body Report, *US-Corrosion Resistant Steel Sunset Review*, para 81

¹²⁴ See e.g. Panel report, *Japan-Film*, paras. 10.43-10.44, which read "[T]he ordinary meaning of measure as it is used in Article XXIII:1(b) certainly encompasses a law or regulation enacted by a government. But in our view, it is broader than that and includes other governmental actions short of legally enforceable enactments.(225) At the same time, it is also true that not every utterance by a government official or study prepared by a non-governmental body at the request of the government or with some degree of government support can be viewed as a measure of a Member government. In Japan, it is accepted that the government sometimes acts through what is referred to as administrative guidance. In such a case, the company receiving guidance from the Government of Japan may not be legally bound to act in accordance with it, but compliance may be expected in light of the power of the government and a system of government incentives and disincentives arising from the wide array of government activities and involvement in the Japanese economy."

defendant and has an obvious impact on his behaviour. Any investigation opened by the DOJ would therefore be relevant for our purposes.

The analysis below will show that the US laws "as such" could be "measures" subject to challenge in the present case in the same way as they were in *US-Gambling*, but that in the event of a withdrawal of the US GATS gambling and betting commitments, the US laws "as applied", as well as – to the extent that they are not captured by the "as applied" challenge- the individual enforcement actions against EC suppliers as separate, autonomous measures could become the main focus of a potential challenge.

C.4.2. *The US commitments under the GATS*

The Panel in *US-Gambling* found that the US schedule under the GATS included specific commitments on gambling and betting services. This finding was later upheld by the Appellate Body.¹²⁵ Even if this inclusion had happened perhaps inadvertently, as the Panel commented, "the scope of a specific commitment cannot depend upon what a Member intended or did not intend to do at the time of the negotiations";¹²⁶ and "independent from any expectation or any unintentional mistake, the United States' obligations pursuant to Article XVI.4 (of the WTO Agreement) are to ensure that its relevant laws are in conformity with its WTO obligations, including any commitments undertaken in its GATS Schedule."¹²⁷ There is no need therefore to dwell on this question.

However, the US notified on 8 May 2007 its intention pursuant to Article XXI of the GATS to modify, in part, its commitment on "Other Recreational Services" in its schedule, by excluding gambling and betting services from its subsector coverage. The notice of initiation¹²⁸ of this examination procedure summarised the argumentation in the complaint on this matter as follows:

"The complainant gives consideration as well to the fact that the relevant GATS legal framework is expected to undergo significant changes in the coming months as a result of the intention of the US to withdraw its GATS commitments on gambling and betting services. The complainant argues that this withdrawal would not have retroactive effects, and would therefore not affect the US obligations in respect of any act or fact occurred while the commitment was still in place. Given that the only relevant trade ("act or fact") at issue in the complaint is the remote gambling that a number of EU based operators offered to persons in the US prior to their withdrawal from the US market, and therefore while the US commitments were in place, the US would according to the complainant be under the obligation not to take or continue any measure that would constitute a violation of its obligations in relation to such past trade."

¹²⁵ Panel Report, *US – Gambling*, para. 6.134; Appellate Body Report, para. 213.

¹²⁶ Panel Report, *US – Gambling*, para. 6.136

¹²⁷ Panel Report, *US – Gambling*, para. 6.138

¹²⁸ Notice of Initiation of an examination procedure concerning obstacles to trade within the meaning of Council Regulation (EC) No 3286/94 consisting of the US ban on foreign internet gambling and its enforcement (2008/C 65/07) (OJ C 65, 11.3.2008, p. 5).

The US commitments on gambling and betting services were still in place at the time of concluding the drafting of this report. However, it is likely for the ongoing procedure under Article XXI of the GATS to deliver, sooner or later, the withdrawal of the US commitments. The question that the Commission services consider appropriate to address is whether this withdrawal would have any impact, and if the answer is positive, which impact, on the EC right of action under international trade rules in the sense of the Trade Barriers Regulation in respect of the US measures at stake.

Apart from Article XXI, the following WTO provisions appear as particularly relevant for this analysis: Article XXIII:1 of the GATS; Article 3.8 of the DSU; and Article 19.1 of the DSU.

Article XXIII:1 of the GATS provides as follows:

"If any Member should consider that any other Member fails to carry out its obligations or specific commitments under this Agreement, it may with a view to reaching a mutually satisfactory resolution of the matter have recourse to the DSU."

Article 3.8 of the DSU provides as follows:

"In cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered prima facie to constitute a case of nullification or impairment. This means that there is normally a presumption that a breach of the rules has an adverse impact on other Members parties to that covered agreement, and in such cases, it shall be up to the Member against whom the complaint has been brought to rebut the charge."

Article 19.1 of the DSU provides as follows:

"Where a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned bring the measure into conformity with that agreement. In addition to its recommendations, the panel or Appellate Body may suggest ways in which the Member concerned could implement the recommendations."

As described in more detail in section D.2 of this report, all EU companies that had been active on the US remote gambling and betting market left it definitively at the end of 2006. EU suppliers of gambling and betting services therefore no longer offer services on the US market.

Their withdrawal from the US market notwithstanding, a number of EU suppliers are under investigation by the DOJ in relation to the gambling and betting services offered while active on the US market. It is therefore clear that, even if the US succeeded in withdrawing its GATS commitments on gambling and betting services at some point in the future, the trade in services at stake in this case took place at a time when the US had specific commitments on gambling and betting services under the GATS.

It is clear that the US (as well as any other Member) must abide by whatever obligations and commitments are applicable at the time where the relevant trade flow under consideration is taking place. Therefore, to the extent that the US takes actions in respect of such past trade, it has in so doing to comply with such applicable obligations and commitments. Any action by the US in respect of past trade that does not take account of

the applicable obligations and commitments would imply a failure on its part to "carry out its obligations or specific commitments" and "an infringement of the obligations" that it has assumed under the GATS.

We will now examine in more detail the reasons why the withdrawal of its GATS commitments by the US would not affect its obligations in respect of past trade, and why, as a result, its measures could still be challenged even after the withdrawal of the US GATS commitments on gambling and betting services.

C.4.2.1. Article XXI of the GATS

Article XXI:2 (a) of the GATS reads as follows:

"At the request of any Member the benefits of which under this Agreement may be affected (referred to in this Article as an "affected Member") by a proposed modification or withdrawal notified under subparagraph 1(b), the modifying Member shall enter into negotiations with a view to reaching agreement on any necessary compensatory adjustment. In such negotiations and agreement, the Members concerned shall endeavour to maintain a general level of mutually advantageous commitments not less favourable to trade than that provided for in Schedules of specific commitments prior to such negotiations."

The wording of Article XXI implies that the compensatory adjustment to be negotiated should consist of new commitments that would replace the commitments withdrawn, with the effect that the general level of the commitments after the withdrawal will not be less favourable than before. In other words, the conditions for trade in services shall not, as a result of the withdrawal, become less favourable to trade. If new commitments replace old commitments, it follows that the new commitments will apply for the future, while the old commitments will remain relevant for the past. It is obvious that the new commitments and obligations will not apply in respect of the past. For example, if a new commitment grants market access in a sector previously closed to foreign operators, it is clear that foreign operators will not be able to complain for the lack of access while the commitment was still not in place. Conversely, the withdrawal of a commitment will only have effects for the future; Members would not be able to act as if the relevant obligations had never existed. The same conclusion can be drawn from the examination of the "Procedures for the Implementation of Article XXI of the GATS" (S/L/80), and *mutatis mutandis*, also from Article XXVIII of the GATT and from the relevant Understanding.¹²⁹

C.4.2.2. Non-retroactivity of Treaties

The principle of non-retroactivity of Treaties is codified in Article 28 of the Vienna Convention,¹³⁰ which reads:

"Unless a different intention appears from the treaty or is otherwise established, its provisions do not bind a party in relation to any act or fact

¹²⁹ Understanding on the Interpretation of Article XXVIII of the GATT 1994

¹³⁰ Vienna Convention on the Law of the Treaties, 1969. United Nations, Treaty Series, vol. 1155, p. 331

which took place or any situation which ceased to exist before the date of the entry into force of the treaty with respect to that party."

This principle implies that an amendment to a treaty, such as the modification of commitments undertaken under the GATS, shall also "not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of entry into force" that is, shall not have any retroactive effects. This would only be otherwise if a different intention appeared from the treaty, or was otherwise established.

Similarly, to the extent that a withdrawal of commitments aims at removing certain obligations, it could not be argued that the obligations are removed also in respect of any act or fact, or any situation, which existed before the entry into force of the amendment. In other words, a withdrawal of commitments under the GATS cannot have retroactive effects. This is further confirmed by the fact that, as discussed in the previous section, "no such intention appears from the treaty."

Even if the US would no longer be bound by its GATS obligations in respect of gambling and betting trade that takes place after the withdrawal of commitments (which are still in the process of being formally changed through the Article XXI procedure), the US would still continue to be bound by its GATS obligations which are derived from its (former) commitments in respect of any gambling and betting trade which took place before the withdrawal of its GATS commitments had taken place. As long as there are US enforcement actions relating to trade that took place when the US still had GATS gambling and betting commitments, there would be a "situation which has not ceased to exist – that is...that arose in the past, but continues to exist..."¹³¹ which could also be described as a "continuing measure". This is referring to the enforcement of the US prohibition against EU suppliers in respect of gambling and betting trade that took place while the US GATS commitments were still in place, which could thus be scrutinised by a WTO panel. This scrutiny would have to be based on the GATS commitments in place at the time of the relevant trade flows.

C.4.2.3. Articles XXIII:1 of the GATS and 3.8 of the DSU

Both these articles deal with the issue of standing to challenge an infringement of the obligations undertaken under an agreement. In this particular case, the US would be under the obligation in accordance with the GATS to respect its commitments on gambling and betting services, and not to take (or continue to take) any measure that would be inconsistent with its obligations. Given that its obligations would include abiding by its commitments in respect of any act or fact or situation that took place or existed while the commitments were in place, it would be possible for the EC to "challenge an infringement" even after the withdrawal of the US commitments.

¹³¹ See in this respect Appellate Body report, *Canada-Patent Term*, para. 72: "... Article 28 [of the Vienna Convention on the Law of Treaties] establishes that, in the absence of a contrary intention, treaty provisions do not apply to "any situation which ceased to exist" before the treaty's entry into force for a party to the treaty. Logically, it seems to us that Article 28 also necessarily implies that, absent a contrary intention, treaty obligations do apply to any "situation" which has not ceased to exist — that is, to any situation that arose in the past, but continues to exist under the new treaty. ..."

C.4.2.4. Article 19.1 of the DSU

In accordance with Article 19.1 of the DSU, it is necessary for a measure to exist and for it to be inconsistent with a covered agreement in order for a panel or the Appellate Body to recommend that the measure be brought into conformity with the relevant covered agreement. The Appellate Body concluded the following in this respect in *US-Certain EC products*:

"[T]here is an obvious inconsistency between the finding of the Panel that "the 3 March Measure is no longer in existence" and the subsequent recommendation of the Panel that the DSB request that the United States bring its 3 March Measure into conformity with its WTO obligations. The Panel erred in recommending that the DSB request the United States to bring into conformity with its WTO obligations a measure which the Panel has found no longer exists."¹³²

In this case, there is a "continuing measure" that existed both before and (depending on the outcome of ongoing article XXI negotiations) after the withdrawal of the US commitments on gambling and betting services. One should note that there would still be such a "continuing measure" if the US launched new enforcement actions against EC companies after the withdrawal of its GATS commitments on gambling and betting services, for as long as the new enforcement actions relate to trade that took place while the US gambling and betting commitments were in place. As a result, and for as long as enforcement actions against EC companies remain active, a "measure" would still be "in existence" at the time of examination -and would continue into the past, into the time when US commitments were in place.

Obviously, the withdrawal of the US commitments would have an impact on the definition of the "measure" at stake, and would clearly have an impact on the remedy that the panel or Appellate Body may recommend. Regarding the latter issue, there would be obvious difficulties, including systemic ones, with pushing for a remedy that could have implications for past effects of the measures at stake. This is something that WTO jurisprudence has been careful to avoid, for example the Panel in *Guatemala-Cement II*:

"In respect of Mexico's request that we suggest that Guatemala refund the anti-dumping duties collected, we note that Guatemala has now maintained a WTO-inconsistent anti-dumping measure in place for a period of three and a half years. ... Mexico's request raises important systemic issues regarding the nature of the actions necessary to implement a recommendation under Article 19.1 of the DSU, issues which have not been fully explored in this dispute. Thus, we decline Mexico's request to suggest that Guatemala refund the anti-dumping duties collected."¹³³

It is also relevant to recall what the EC claimed before the panel in *EC-Geographical Indications (DS 290)*:

¹³² Para. 81

¹³³ Panel Report, *Guatemala-Cement II*, para. 9.7

"The European Communities considers it important to remark that Australia is seeking a retroactive remedy that it could not have obtained had it attacked the measure while it was still in force. It submits that it is universally accepted that Article 19.1 of the DSU signifies that the recommendations of panels and the Appellate Body are prospective, not retrospective, in nature. Even if Australia had challenged the Regulation before it was amended, it could not have claimed that the European Communities undo all the registrations already carried out or reopen a possibility of objection against such registrations or provide compensation."¹³⁴

Moreover, there would be a specific difficulty derived from the features of this case regarding the temporal application of rights and obligations. Even if the "measures" under challenge were found not to be in conformity with the GATS given the commitments applicable at the time of the relevant trade, some of the measures would probably be in conformity with the GATS as modified after the withdrawal of the relevant commitments. There may be possible ways in which this specific difficulty could, in theory, be addressed (e.g. by enacting a grandfathering provision that would provide a safe harbour from prosecution for services offered under the cover of US GATS commitments; or by stopping enforcement actions against foreign suppliers based on past acts or facts). However, considering the possible options does not make sense at this stage, especially given the likelihood that a recommendation would not include a specific way of bringing the relevant measures into compliance.

This brings us to the issue of how the measure should be defined in order to ensure that, in case of a challenge with a positive outcome, the recommendation would ensure that the WTO-inconsistent "continuing enforcement" of the US gambling laws in respect of past acts or facts is stopped, and this even after the withdrawal of the US GATS gambling and betting commitments.

It results from the foregoing analysis that although US laws could at present be challenged "as such", as was done by Antigua in *US-Gambling*, these same US laws would in the event of a withdrawal of US gambling and betting commitments in principle be, "as such", consistent with the GATS agreement as modified by the withdrawal. That is, to the extent that US laws are not applied in respect of trade that took place while the relevant US commitments were still in place, but only in respect of trade that takes place after the withdrawal, the US laws, "as such" and "as applied", would in principle be WTO-consistent. However, to the extent that these same laws are applied in respect of trade that took place while the relevant commitments were still in place but disregarding these commitments, the US laws, "as applied", would be WTO-inconsistent.

Therefore, and although this does not need to be definitively established in this report, it is clear that while the focus of a potential challenge should be the US laws "as such" in the event of a case under full US GATS gambling and betting commitments, a potential challenge after a withdrawal of commitments would need to focus on the US laws "as applied", and on the specific enforcement actions against EU companies. In conclusion, both the US gambling laws and the specific enforcement actions on the basis of the laws should be part of the specific measures challenged in any potential WTO case.

¹³⁴ Quoted in the panel report, *EC-Geographical Indications*, para. 7.742

C.4.3. Article XVI of the GATS

The prohibition on the cross-border supply of gambling and betting services contained in the Wire Act; the Travel Act; the IGBA; the UIGEA; the PASPA; the ITWA; US legislation on money laundering; the RICO Act; and individual state laws prohibiting remote gambling and betting on a cross-border basis, amounts to a "zero quota"¹³⁵ on service operations or output with respect to such services. As a result, the measures containing this prohibition are incompatible with Article XVI:1 and XVI:2(a) and (c) of the GATS.

Equally, the individual enforcement measures adopted in implementation of this prohibition, which effectively prohibit the cross-border supply of gambling and betting services offered by the individual companies subject to the relevant investigations, are incompatible with Article XVI:1 and XVI:2(a) and (c).

C.4.3.1. Justification under Article XIV of the GATS

To the extent that, in the event of a WTO challenge, the US continues to argue in its possible "affirmative defence" that the prohibition on the cross-border supply of gambling and betting services is part of a total ban on remote gambling, it would be possible to counter that the exceptions in US law and practice that permit significant supply of remote gambling from within the US make a justification under Article XIV impossible. On this basis, and in the light of the outcome of the *US-Gambling* case, one could without any further analysis conclude that the US measures at issue that violate Article XVI of the GATS are not justified under Article XIV.

However, some additional analysis can be useful given, first, the need to consider the reasons why the Appellate Body came to its conclusion regarding Article XIV; and, second, because - as indicated in the complaint - factual developments in the last two years have not only made the violations of Article XVI more clear cut, but also significantly undermined the US position with regard to a possible defence based on Article XIV. Moreover, there is one defence element in Article XIV that the US failed to use in *US-Gambling*: as the Appellate Body put it, "the United States sought to justify the Wire Act, the Travel Act, and the IGBA on the basis that there is *no discrimination*... The United States could have, but did not, put forward an additional argument that *even if* such discrimination exists, it does not rise to the level of "arbitrary" or "unjustifiable" discrimination."¹³⁶

Article XIV of the GATS, like Article XX of the GATT 1994, contemplates a "two-tier" analysis of measures that a Member may seek to justify under that provision.¹³⁷ The "first tier" analysis addresses the question of whether the measure falls within the scope of one of the paragraphs of Article XIV, and therefore whether the measure is "necessary" to achieve the relevant objectives, while the "second tier" considers whether it meets the requirements of the *chapeau* of Article XIV.

¹³⁵ See relevant analysis in Appellate Body report, *US-Gambling*, paras. 214 et seq.

¹³⁶ Appellate Body Report, *US – Gambling*, para. 350 (original emphasis)

¹³⁷ Appellate Body report, *US-Shrimp*, para.147

WTO jurisprudence has stated that whether a measure is "necessary" should be determined through a process of weighing and balancing a series of factors to determine whether a WTO consistent alternative measure, or a less WTO-inconsistent measure, is reasonably available. The process would require considering the relative importance of the interests or values furthered by the measure; the contribution of the measure to the ends pursued; and the restrictive impact of the measure on trade.¹³⁸ It is important to note that this does not imply any limitation on Members' ability to achieve their legitimate objectives: a "reasonably available" alternative measure must be a measure that would preserve for the relevant Member its right to achieve its desired level of protection with respect to the objective pursued.¹³⁹ Also, Members are free to define the public policy objectives that they want to pursue. But, "so far as the WTO is concerned, that autonomy is circumscribed only by the need to respect the requirements of the *General Agreement* and the other covered agreements."¹⁴⁰

Specifically as regards the concept of "public morals" and "public order" in Article XIV(a) GATS, the Panel in *US-Gambling* concluded that measures prohibiting gambling and betting services, including over the Internet, could fall within the scope of the Article if enforced in pursuance of policies the purpose of which is to protect public morals or to maintain public order.¹⁴¹ Specifically, it found that the Wire Act, the Travel Act and the IGBA fell within Article XIV(a)¹⁴² and that, as far as remote supply of gambling and betting services was concerned, these Acts (when read together with the relevant State laws) contributed, at least to some extent, to addressing the ends pursued by those laws, including concerns pertaining to money laundering, organized crime, fraud, underage gambling and pathological gambling.¹⁴³ The Appellate Body did not see any error in this reasoning.¹⁴⁴

There could be, however, a way to challenge this conclusion. One should first note that according to the Appellate Body in *Brazil-Retreated Tyres*, "[A] contribution exists when there is a genuine relationship of ends and means between the objective pursued and the measure at issue. To be characterized as necessary, a measure does not have to be indispensable. However, its contribution to the achievement of the objective must be material, not merely marginal or insignificant, especially if the measure at issue is as trade restrictive as an import ban."¹⁴⁵

It can be argued that the US measures are not a total ban on gambling, but rather a partial and discriminatory ban which, while prohibiting remote supply from third countries, authorizes such supply from within the US on both an intrastate and interstate basis. This

¹³⁸ Appellate Body Report, *Korea – Various Measures on Beef*, paras. 164-166

¹³⁹ Appellate Body Report, *EC – Asbestos*, paras. 172 – 174. See also Panel Report, *US-Gambling*, para. 6.461

¹⁴⁰ Appellate Body Report, *US-Gasoline*, page 30

¹⁴¹ Panel Report, *US-Gambling*, p. 6.474

¹⁴² Panel Report, *US-Gambling*, p. 6.487

¹⁴³ Panel Report, *US-Gambling*, p. 6.494

¹⁴⁴ Appellate Body Report, *US-Gambling*, p. 313

¹⁴⁵ Appellate Body Report, *Brazil-Retreated Tyres*, para. 210

type of partial ban should not be considered to contribute to the objectives pursued. Discriminating against services supplied from third countries does not, in principle and in itself, make any contribution to the ends pursued. In this respect, it is noteworthy to refer to the separate opinion in the Article 22.6 Decision by the Arbitrator in *US-Gambling* that "it is not clear how the United States proposes to reconcile the protection of public morals or public order with the opening of one segment of the market (horseracing)."¹⁴⁶ This would constitute a first way of challenging the necessity of the US measures under Article XIV(a) (and (c)) of the GATS.

There is an additional avenue that could be taken to challenge the "necessity" of the US measures. It is worth recalling that, with regard to the existence of "reasonably available" alternative measures, the Panel in *US-Gambling* found that the US measures under consideration had not passed the "necessity test" in Article XIV GATS, and in this respect indicated that "the responding Member must have first explored and exhausted all reasonably available WTO-compatible alternatives before adopting its WTO-inconsistent measure"¹⁴⁷. This finding was later reversed by the Appellate Body. The reason was that the Panel had not focused on alternative measures that were reasonably available to the US,¹⁴⁸ but only on the fact that the US had not engaged in consultations with Antigua (which are not an "alternative measure", but rather "a process")¹⁴⁹. As a result, the Appellate Body concluded that the US measures were "necessary",¹⁵⁰ but only because the US had made its *prima facie* case on "necessity", while Antigua had failed to identify a reasonably alternative measure.¹⁵¹

The reasoning of the Appellate Body clearly suggests that it may be possible to challenge the affirmative defence of the US by proposing alternative measures which the US could take and which are different from a prohibition but would achieve the same objectives. It would then be up to the US to demonstrate that the proposed alternative is not "reasonably available" in the light of the interests and values being pursued and the US desired level of protection.¹⁵²

In sum, the EC could thus still show that the US approach of prohibiting Internet gambling and betting altogether is not "necessary" in the terms of Article XIV (a) (and (c)) of the GATS, that is, the US measures could still fail the "necessity test" in Article XIV.

This should by no means be excluded. The enactment of UIGEA showed that alternative measures that are WTO consistent (such as authorisation/licensing under sufficiently strict conditions) are reasonably available to the US. One should recall in this respect

¹⁴⁶ 22.6 Decision by the Arbitrator, *US-Gambling*, para. 3.67

¹⁴⁷ Appellate Body Report, *US – Gambling*, para. 315

¹⁴⁸ Appellate Body Report, *US – Gambling*, para. 317

¹⁴⁹ Appellate Body Report, *US – Gambling*, paras. 317-321

¹⁵⁰ Appellate Body report, *US-Gambling*, para. 327

¹⁵¹ Appellate Body Report, *US – Gambling*, para. 326

¹⁵² Appellate Body Report, *US – Gambling*, para. 311

that UIGEA requires compliance of intrastate and intratribal transactions with certain conditions in order to qualify for exclusion from the concept of "unlawful Internet gambling" (e.g. that the relevant laws and regulations include age and location verification requirements, or appropriate data security standards). This was duly noted in the 21.5 Arbitration Award in *US-Gambling*, as a change with respect to the US position submitted to the original Panel that such regulation "was infeasible".¹⁵³

If the EC was successful in showing that the US prohibition is not necessary in the terms of Article XIV(a), it would still need to show that it is not necessary under Article XIV(c) either. In this respect, the Panel in *US-Gambling* found that the US could rely upon the RICO Act in asserting a defence under Article XIV(c), and that the Wire Act, the Travel Act and the IGBA "secured compliance" with the RICO Act.¹⁵⁴ It then concluded that they made a significant contribution to ensuring that law enforcement efforts against organized crime under the RICO Act were not undermined. However, and based on the same reasoning followed under Article XIV(a), it found that the US had not explored and exhausted WTO-consistent alternatives in the form of negotiations or consultations to determine other ways of addressing organized crime concerns, and that the US measures were, as a result, not "necessary".

Although the Appellate Body exercised judicial economy with respect to the analysis under Article XIV(c), it is obvious that it would have reached the same conclusion that it reached with regard to XIV(a), namely that "consultations" are not an "alternative measure", but rather a "process". The EC would therefore need to show that alternative measures are "reasonably available" to the US in order to prove that the US ban is not "necessary" under Article XIV(c) GATS.

It is not necessary at this stage to enter into a detailed analysis of the potential "alternative measures" available to the US. This should nonetheless not pose unsurmountable difficulties. Suffice it to refer to two ideas:

- First, the conditions - proposed by UIGEA - that regulated remote gambling services need to meet in order for them to be excluded from "unlawful Internet gambling" presumably meet (either in themselves or in combination with other measures) the US policy objectives with regard to organized crime and other public policy objectives. If it is possible to meet these objectives via regulation for US-based services, it should also be possible to meet them for services provided from abroad.
- Second, as observed by the separate opinion in the Article 22.6 Decision by the Arbitrator in *US-Gambling*, "it is quite conceivable that the United States could have found ways in which to address these concerns while protecting such interests. Other WTO Members have chosen to open their market to remote gambling, and it would not be reasonable to assume that such Members do not also have similar policy concerns."¹⁵⁵ Also, one should note again in this respect the observation in the 21.5 Arbitration Award in *US-Gambling* quoted above, that the UIGEA requirement for regulations to include age and location verification systems represented a change with

¹⁵³ Article 21.5 Panel Report, *US-Gambling*, footnote 195

¹⁵⁴ Panel Report, *US-Gambling*, paras. 6.551 and 6.554 to 6.556

¹⁵⁵ 22.6 Decision by the Arbitrator, *US-Gambling*, para. 3.69

respect to the original US position submitted to the original Panel that such regulation was unfeasible.

With regard to the "second tier" analysis, which deals with the question of how the relevant measures are applied, the Appellate Body in *US-Gambling* found that the US had not demonstrated, in the light of the IHA, that the prohibitions in the Wire Act, the Travel Act and the IGBA applied to both foreign and domestic suppliers of remote betting services for horse racing.¹⁵⁶

Developments since then add new arguments to further weaken the US position with regard to the requirements in the *chapeau*.

- First, it is worth noting that the Panel originally found that the US was not acting in accordance with the chapeau of Art. XIV GATS also because it was not taking enforcement actions against a number of large-scale internet gambling operators, but had acted against an Antigua-based operator. The Appellate Body reversed the Panel findings in this respect because it considered that it had wrongly assessed the available evidence by considering a few isolated instances of enforcement (or lack thereof) as sufficient to rebut the US defence and warrant a finding of "inconclusiveness". However, even if this was the case in *US-Gambling*, it is not excluded that the additional enforcement evidence that has become –and may still become - available since then could be sufficient to prove discrimination for the purposes of the *chapeau*.
- Second, although the Appellate Body in *US-Gambling* did consider the IHA as a source of discrimination,¹⁵⁷ it failed to consider an additional source of discrimination, namely the fact that the Wire Act, the Travel Act and the IGBA do not apply to intrastate commerce. The Article 21.5 Panel Report in *US-Gambling* clearly points at a further serious GATS violation in this respect. It hinted at it in the statement that "the Wire Act (and the Travel Act) discriminate on their face between services supplied within the United States and those supplied from outside the United States, insofar as they do not apply to services not supplied in interstate or foreign commerce".¹⁵⁸ In so doing, the 21.5 Panel justifiably proved wrong the Appellate Body's express findings ("these measures, on their face, do not discriminate between United States and foreign suppliers of remote gambling services"), which it quotes in its Report in implicit disagreement.¹⁵⁹ This is very relevant in that it shows that there is a *de iure* discrimination that applies across the board (i.e. not only with regard to horse racing), given that the alleged US ban does not extend to intrastate commerce. This is confirmed by the fact that, according to Antigua's arguments, at least 18 State laws expressly authorize remote gambling, in some cases beyond horse racing¹⁶⁰. This additional aspect not only contributes to casting very serious doubts regarding the existence of a general ban on internet gambling in the US. It also makes it virtually

¹⁵⁶ Appellate Body Report, *US – Gambling*, para. 372

¹⁵⁷ Appellate Body Report, *US – Gambling*, para. 348

¹⁵⁸ Article 21.5 Panel Report, *US – Gambling*, paras. 5.27 and 6.121 to 6.123

¹⁵⁹ See footnote 184, Article 21.5 Panel Report, *US – Gambling*

¹⁶⁰ Article 21.5 Panel Report, *US – Gambling*, para. 6.121

impossible that the US ban could be justified under the *chapeau* of Article XIV of the GATS.

With regard to the possibility for the US to argue that, if there was discrimination, it would not be "arbitrary" or "unjustifiable", this would probably only be relevant if the DOJ changed its longstanding position and accepted that US federal law is, indeed, discriminatory. It is not possible to argue simultaneously that US law does not, on its face, discriminate, and at the same time provide reasons why its discriminatory aspects are neither "arbitrary" nor "unjustifiable". Should the US unexpectedly change opinion and accept that its legislation is discriminatory (mainly because of the IHA and of the exclusion on intrastate gambling), it would still be close to impossible for the US to convincingly argue that it would not be applying its measures "arbitrarily" or "unjustifiably" when excluding foreign operators from remotely supplying gambling and betting services on horse racing (or other gambling services also offered remotely on an intrastate basis), while at the same time allowing local suppliers to provide those services through the same technological means and with equivalent safeguards to ensure "socially responsible" gambling. Moreover, one has to recall the separate opinion in the Decision by the Arbitrator under Article 22.6 of the DSU according to which "in this case (something which is not within our mandate to determine), it is not clear how the United States proposes to reconcile the protection of public morals or public order with the opening of one segment of the market (horseracing)."¹⁶¹

This does not mean that discrimination would not be acceptable in some cases. To the contrary, discrimination may in specific instances be justified. As noted by the EC in its Third Party Submission in *US-Gambling*, "formally different treatment based on different circumstances in the Member from which the service is provided, inasmuch as those circumstances had an impact on the market of the Member whose measure is at issue, might also be relevant under Article XIV of the GATS."¹⁶²

However, this can hardly be the case as far as the EU companies covered by this investigation are concerned, which are licensed to operate in EU jurisdictions and therefore meet the relevant regulatory obligations, including provisions on social responsibility in the operation of remote gambling and in advertising. Moreover, several of the companies are listed on stock exchanges across the EU, notably on the London Stock Exchange, with the corresponding obligations resulting thereof.

In conclusion, the challenged measures could not be justified on the basis of Article XIV of the GATS.

C.4.4. *Article XVII of the GATS*

As indicated above, the choice of the complainant was to focus its analysis on the US authorities' own interpretation of the relevant laws. This interpretation can be summarised in the DOJ belief that current US federal law, including 18 U.S.C. §§ 1084, 1952, and 1955, prohibits all types of gambling over the Internet ("The DOJ approach").

¹⁶¹ 22.6 Decision by the Arbitrator, *US-Gambling*, para. 3.67

¹⁶² Para. 54

There is, however, an alternative approach, based on the interpretation that current US law does not prohibit all types of gambling over the Internet. On the contrary, US law would permit the supply of substantial remote gambling and betting services, both on an interstate and an intrastate basis, but only to US service suppliers. We will consider these two alternative approaches in turn.

C.4.4.1. The DOJ approach

The interpretation put forward by the DOJ is that there is a total prohibition on the supply of any gambling and betting service over the Internet. It is also the view of the US Administration and the DOJ that, to the extent that state laws purport to legalize or permit certain instances of gambling and betting services over the Internet, the prohibitions contained in federal law would prevail.¹⁶³ As a result, US law would not, as such, contain any discrimination against foreign suppliers.

(a) "Likeness across modes"

Still, even this interpretation of US laws could be challenged under Article XVII of the GATS. The claim would be based on the fact that US laws permit the supply of off-line, "bricks and mortar" gambling and betting services to US suppliers, but not cross-border services supplied over the Internet. The key argument to be made would be that Internet-based services are "like" off-line gambling and betting services. In fact, Antigua argued along these lines in *US-Gambling*,¹⁶⁴ maintaining that "the fact that services of Antiguan gaming operators are supplied via a different "mode of supply" than services of suppliers of United States origin (cross-border as opposed to commercial presence) does not make these "unlike."¹⁶⁵

This is of course true, and in fact WTO jurisprudence has in *Canada-Autos* indeed accepted¹⁶⁶ the possibility of "likeness across modes". The main argument in favour of "likeness across modes" is that the text of GATS Article XVII does not suggest that the mode of supply is relevant for defining likeness. However, this has to be weighed against the logic and structure of the GATS, because of the implication that "[I]n its most extreme form, it would mean that, in a given sector, a Member would not be able to undertake different levels of national treatment commitments for the different modes; or that, by virtue of a commitment under a certain mode (mode 3, for instance), suppliers under other modes could claim national treatment, irrespective of whether there is a relevant commitment. This approach would be hard to reconcile with Members' agreed

¹⁶³ "The DOJ, however, does not view this provision as codifying the legality of common pool wagering and interstate account wagering even where such wagering is legal in the various States involved for horseracing". Statement by President Clinton on 21 December 2000 accompanying the signing of H.R 4942, the Act amending the IHA and arguably establishing a "safe harbour" for horse racing

¹⁶⁴ The question of "likeness" was not addressed in *US-Gambling*, for reasons of judicial economy. See panel report, para. 6.287

¹⁶⁵ Quoted in Panel Report, *US-Gambling*, para. 3.150

¹⁶⁶ "In our view, it is reasonable to consider for the purposes of this case that services supplied in Canada through modes 3 and 4 and those supplied from the territory of other Members through modes 1 and 2 are 'like' services." Panel report, *Canada-Autos*, para. 10.307

practice to schedule commitments mode by mode."¹⁶⁷ This calls for a cautious, case-by-case approach.

In this sense, the EC in *EC-Gambling* stated that it shared "the Appellate Body's view on the need for a case-by-case approach to the issue of "likeness" in WTO provisions. Furthermore, some special caution needs to be exercised to avoid mechanical transposition to services of criteria developed in connection with trade in goods. Services are, generally, a different "case".¹⁶⁸ The EC further noted that "paragraph 3 of Article XVII expressly refers to a modification of the conditions of competition (to the detriment of foreign services and suppliers) as an indication of "less favourable treatment". This provision suggests that the purpose of the GATS national treatment obligation is to protect the expectations of equal competitive conditions between foreign and domestic services and suppliers [In a footnote in the original: similarly to Article III of GATT 1994 (see Appellate Body Report on *EC – Asbestos*, paras. 98-99, referring to the Appellate Body Report on *Japan – Alcoholic Beverages II*, paras. 109-110)]. A notion of "likeness" that were so narrow such that it would not be permissible to take account of the competitive relationship between foreign and domestic services would not seem to be in line with the full text and objective of Article XVII."¹⁶⁹

In this particular case, the issue of the "means of delivery" of the service seems relevant to the analysis. This issue was dealt with in their analysis under Article XVI by both the panel and the Appellate Body in *US-Gambling*, with the conclusion that "mode 1 under the GATS encompasses all possible means of supplying services from the territory of one WTO Member into the territory of another WTO Member. Therefore, a market access commitment for mode 1 implies the right for other Members' suppliers to supply a service through all means of delivery, whether by mail, telephone, Internet etc., unless otherwise specified in a Member's Schedule."¹⁷⁰

When addressing the question of "likeness" in this case, it seems thus logical to give a particular weight to the treatment of remote supply by local services and service suppliers. A comparison of the same "means of delivery" across different modes appears as absolutely relevant.¹⁷¹ If this variable is not factored into the equation, the outcome can become unreasonable: local services and service suppliers could be prohibited from supplying gambling and betting services via the Internet, but foreign services and service suppliers would be entitled to cross-border access, including via the Internet, based on

¹⁶⁷ "Determining "likeness" under the GATS: squaring the circle?", Mireille Cossy, Economic Research and Statistics Division, World Trade Organization

¹⁶⁸ Panel Report, *US-Gambling*, para. 4.36

¹⁶⁹ Panel Report, *US-Gambling*, para. 4.40

¹⁷⁰ Panel Report, *US-Gambling*, para. 6.285

¹⁷¹ See in this respect Cossy, p. 15: "The concept of "likeness across modes" seems to rest on a confusion between "modes" and "means" of supply. There is no "mode" of supply for national products and producers. In fact, the real question is whether the means of supply (electronic transaction vs. "face-to-face", for example) should, as such, play a role in the determination of likeness. The answer will involve a series of questions closely related to the supplier of the service. A proper standard for comparison remains to be established between foreign and national services and suppliers, based on a series of criteria which most likely will have to factor in the means through which a service is supplied. The national treatment obligation must be given a meaning for – and within – each modes of supply, independently from the other modes."

their "likeness" to off-line local services and service suppliers and the consequent applicability of the national treatment obligation.

In conclusion, given the importance that the means through which the service is supplied is bound to have in any discussion of "likeness" in this particular case, and the likelihood that, as a result, off-line gambling and betting services would not be considered "like" online services, it does not seem appropriate to pursue this argument any further.

(b) "Practice" of discriminatory enforcement

If US law did not, as such, contain any discrimination against foreign remote suppliers, the possibility would still exist that the DOJ would be enforcing the general ban on remote supply selectively against foreign suppliers, and that this selective enforcement could rise to the level of discrimination in the sense of Article XVII of the GATS. In this respect, the ongoing enforcement actions by the DOJ could theoretically, as indicated in section C.4.1 above, be challenged in and of themselves as a discriminatory "practice".

This approach would require to present sufficient evidence showing that the DOJ is enforcing the ban in a way that results in a repeated pattern of discrimination. At the same time, and in order for the evidence to be relevant, the various enforcement actions would need to be placed in their context, including evidence on the overall number of suppliers, enforcement patterns or reasons for particular instances of non-enforcement.

There is in our view sufficient evidence available to show that, despite its well known position that all types of Internet gambling are prohibited, the DOJ does not act against US suppliers of remote gambling and betting services, notably in the area of horse racing and dog racing. There are, however, sufficient reasons not to further develop an Article XVII claim based on a "practice" of discriminatory enforcement in this case:

- First, the Appellate Body has not so far pronounced on the matter of whether a "practice" can be considered as an autonomous measure. Although this does not rule out the possibility that a practice could be challenged as such, it does imply that the threshold required to make a *prima facie* case would be relatively high.
- Second, the Panel and the Appellate Body in *US-Gambling* found that the US had not demonstrated that –in the light of the existence of the IHA- the Wire Act, the Travel Act and the IGBA were applied consistently with the requirements of the chapeau i.e. in a non-discriminatory way. The Appellate Body upheld the Panel finding by stating that "the evidence provided by the United States was not sufficiently persuasive to conclude that, as regards wagering on horse racing, the remote supply of such services by domestic firms continues to be prohibited notwithstanding the plain language of the IHA."¹⁷² Although the Panel finding was one of "inconclusiveness" given the ambiguity as to the relationship between, on the one hand, the IHA, and the Wire Act, the travel Act and the IGBA on the other, the Panel commented that it agreed with Antigua that the text of the IHA appeared, on its face, to permit interstate pari-mutuel wagering over the telephone or other modes of electronic communication, which presumably would include the Internet, as long as such wagering is legal in both states.¹⁷³ Also, according to the 21.5 Arbitration Award, the supplementary

¹⁷² Appellate Body Report, *US – Gambling*, para. 364

¹⁷³ Panel Report, *US – Gambling*, para. 6.599

evidence submitted in the compliance proceeding "*confirms* that, under US domestic law, whilst repeals by implication are not favoured, they are possible where there is a positive repugnancy between two Acts".¹⁷⁴

- Third, the 21.5 Arbitration Award indicates that "[A]s long as this ambiguity remains, the measures at issue are not in compliance with the United States' obligations under the GATS. Moreover, it adds in footnote 120 that "[T]he Panel's findings are without prejudice to any other possible inconsistencies between the measures at issue and the United States' obligations under the GATS." This is all the more relevant given the 21.5 Panel comments regarding intrastate commerce, which suggest that the drafters were indeed convinced that the original Panel could have made findings of discrimination regarding the Wire Act, State laws and intrastate commerce, in addition to those regarding the ambiguity in the relationship between the IHA and the Wire Act.¹⁷⁵
- Fourth, the text of UIGEA, enacted in October 2006, incorporates a definition of "unlawful Internet gambling" which "excludes certain activities, among them certain intrastate transactions, certain intratribal transactions, and also activities that are allowed under the IHA"¹⁷⁶ This is important not only because it confirms that interstate Internet gambling under the IHA may be possible under the US system, but also because it points at the possibility that intrastate as well as intratribal or even intertribal (i.e. between Indian lands, if allowed by the Indian Gaming Regulatory Act)¹⁷⁷ gambling could be authorized in the US.
- Fifth, the interpretation that remote gambling on horse racing (and dog racing) offered by US suppliers is indeed allowed in the US is widely shared among both US remote gambling suppliers, and horse and dog racing interests in the US. This is clearly shown by the comments filed on UIGEA implementing rules.

Given the likelihood that any pattern of discriminatory enforcement would be attributed to the fact that US law appears to be, on its face, discriminatory, and that as a result a "practice of discrimination" could not, as such, be established, it does not seem appropriate to focus on challenging a "practice" of discriminatory enforcement as such. This should only be done as an alternative claim to the main claim that US law discriminates, on its face, against foreign services and service suppliers.

C.4.4.2. US law is discriminatory

As indicated by the EC in *US-Gambling*, once it is established that the US schedule includes commitments on gambling and betting services, establishing a violation of Article XVII GATS requires assessing "whether there are like services/suppliers; and (...) whether maintaining such measure amounts to less favourable treatment than

¹⁷⁴ Article 21.5 Panel Report, para. 6.109

¹⁷⁵ Article 21.5 Panel Report, para. 6.122

¹⁷⁶ Article 21.5 Panel Report, *US – Gambling*, para. 6.131

¹⁷⁷ UIGEA

granted to domestic services and suppliers, that is (a) whether the measure modifies the conditions of competition and (b) this is in favour of domestic services and suppliers."¹⁷⁸

The question of whether the US schedule includes commitments on gambling and betting services has already been discussed above. The analysis below will therefore focus on the question of likeness of services and service suppliers, and on the question of whether the US measures amount to less favourable treatment.

(a) US services and service suppliers are "like" foreign services and service suppliers

The question of "likeness" in the GATS context has been addressed only partially in WTO jurisprudence so far. It is therefore difficult to provide definitive answers on the question of likeness. The objective of the Commission services will be to show that an Article XVII case can be made. Therefore, the Commission's argumentation will focus on circumstances where "likeness" would be relatively straightforward to establish. Obviously, this does not exclude that a case of likeness could also be successfully constructed in respect of less clear-cut circumstances, and that this might be considered if and when a WTO case on this matter is brought.

In the two cases¹⁷⁹ in which this question has been addressed so far, "likeness" was established on the basis of the similarity of the activity performed and of the result of such activity (i.e. the service itself). As noted by the EC in *Canada-Autos*, determining that a service is "unlike" and would thus warrant a different treatment would require an analysis of "the nature and characteristics of the services themselves". This reflects the line taken by the Panel in *EC-Bananas III* in a finding not reviewed by the Appellate Body, according to which "[T]he nature and the characteristics of wholesale transactions as such, as well as of each of the different subordinated services mentioned in the headnote to section 6 of the CPC, are 'like' when supplied in connection with wholesale services, irrespective of whether these services are supplied with respect to bananas of EC and traditional ACP origin, on the one hand, or with respect to bananas of third-country or non-traditional ACP origin, on the other. Indeed, it seems that each of the different service activities taken individually is virtually the same and can only be distinguished by referring to the origin of the bananas in respect of which the service activity is being performed. Similarly, in our view, to the extent that entities provide these like services, they are like service suppliers."¹⁸⁰

In *EC-Asbestos*, the Appellate Body recalled that the approach for analyzing "likeness" that had been developed over time under the GATT involved assessing "(i) the physical properties of the products; (ii) the extent to which the products are capable of serving the same or similar end-uses; (iii) the extent to which consumers perceive and treat the products as alternative means of performing particular functions in order to satisfy a particular want or demand; and (iv) the international classification of the products for tariff purposes."¹⁸¹ However, as observed by the EC in *US-Gambling*, the Appellate

¹⁷⁸ Panel Report, *US-Gambling*, para. 4.36

¹⁷⁹ *EC-Bananas III* and *Canada-Autos*

¹⁸⁰ Panel Report, *EC - Bananas III*, para. 7.322

¹⁸¹ Appellate Body Report, *EC-Asbestos*, para. 101

Body on that occasion had also emphasized the importance of the physical characteristics of the product – that is the "attributes" or "features" of the product *per se*, which deserved separate examination because they could influence the other "likeness factors". The EC concluded that "[F]ocusing on the "attributes" or "features" of a service *per se*, that is on the activity in which the provision of a service consists and on the result of such activity, seems even more important for services. Their intangible characteristic makes more objectively assessable indicators particularly useful."¹⁸² As a result, "[A]ctivities which are essentially the same...will most likely lead to a finding of "likeness"".¹⁸³

The activity at stake in the present case is the supply of gambling and betting services via remote communication, and notably via the Internet. The Commission services have already concluded in section C.4.4.1.(a) above that, in this particular case, gambling and betting services provided remotely would not in principle be considered "like" off-line gambling and betting services. In addition, and specifically with respect to the "characteristics" of the services involved (online vs. offline), one should note that when commenting on the Panel's finding that the remote supply of gambling services gave rise to particular concerns, the Appellate Body in *US-Gambling* observed that the approach of distinguishing remote from non-remote supply when analysing discrimination in the application of the Wire Act, the Travel Act and IGBA merely reflected "the view that the distinctive characteristics of the remote supply of gambling services may call for distinctive regulatory methods, and that this could render a comparison between the treatment of remote and non-remote supply of gambling services inappropriate." Even if this was a distinction drawn in the context of an Article XIV analysis, it does support the view that online gambling services are not "like" offline gambling services.

Conversely, and given that the relevant activity, including the technological means used, is the same, the Commission services consider that US services consisting of the supply of gambling and betting services via remote communication, and notably via the Internet are "like" the same services supplied from the territory of the EU. There is no question that this is the case when US and EU services are provided on the same subject matter (e.g. horse racing; other sports betting; poker; etc.) In this sense, the EC remarked in its Third Party Submission *US-Gambling* that "[A]t any rate, inasmuch as a prohibition on cross-border supply of gambling and betting services applied across the board to any such services, it would inevitably affect services that are "like" certain domestic ones (for example, phone or internet gambling)."¹⁸⁴ Also, and specifically on the question of the subject matter on which the services are being provided by EC and US suppliers, the EC indicated in the *US-Gambling* proceedings that "if the competitive relationship is distorted, (or absent) owing to a measure applied in the territory into which the service is being supplied, the relevant benchmark is the potential competitive relationship that would exist if the services supplied were not subject to that measure".¹⁸⁵ In conclusion, there is "likeness" between certain US and EU services.

¹⁸² Oral Statement of the EC, *US-Gambling*, para. 29

¹⁸³ Oral Statement of the EC, *US-Gambling*, para. 31

¹⁸⁴ Third Party Submission of the European Communities, *US-Gambling*, para. 98

¹⁸⁵ EC response to Panel questions, Panel Report, *US-Gambling*, Annex C

The remaining question to be addressed is whether these same services, when provided on a different subject matter, would still be "like" services, or rather "unlike" services. Again quoting the EC Third Party Submission in *US-Gambling*, "[I]f differences in the factual circumstances had an impact e.g. on the characteristics of the services themselves, as they are provided in the territory of the WTO Member whose measure is at issue, they could have an impact on the "likeness" of the domestic and foreign service."¹⁸⁶ This is a complex factual issue that needs not be addressed at this stage, given that we have already been able to conclude that at least some EU services are "like" the equivalent US services.

(b) US measures amount to less favourable treatment

In the present case, the available factual evidence supports the assumption that, in the US, gambling and betting services on horse racing (and dog racing) - as well as on other sports at least in the case of Nevada - supplied by remote means are authorized on an intrastate and interstate basis, but not on a cross-border basis from other WTO Members.

The "less favourable treatment" standard was developed through GATT jurisprudence, which clarified that "treatment no less favourable" requires effective equality of competitive opportunities for foreign and domestic goods. This approach, developed and consistently used in the goods area,¹⁸⁷ was codified in Article XVII:2 and 3 of the GATS. "No less favourable treatment" may, in accordance with Article XVII:2 GATS, imply formally different treatment of domestic and foreign services. However, as noted in the EC Third Party Submission in *US-Gambling*, "[O]f course, this would not allow an outright prohibition of foreign services where domestic services are allowed."¹⁸⁸

In the present case, foreign services provided remotely that are the same as domestic services also provided remotely are not allowed into the US market, whereas significant "like" domestic services, provided both intrastate and interstate, are allowed. In line with what the Panel found in *Canada-Autos*,¹⁸⁹ this is bound to have discriminatory effects and is therefore incompatible with Article XVII GATS.

C.4.4.3. Article XIV of the GATS

Article XIV GATS being an "affirmative defence", one would expect the US to continue arguing – as it did in *US-Gambling* - that the relevant US measures, on their face, do not discriminate. As indicated above, the US is likely to defend the prohibition on cross-border supply as part of a total prohibition on remote gambling and betting. If that was the case, then the same conclusions reached in the analysis regarding Article XVI above

¹⁸⁶ Third Party Submission of the European Communities, *US-Gambling*, para. 48

¹⁸⁷ See e.g. Appellate Body Report, *Korea – Various Measures on Beef*, paras. 135-137: "According 'treatment no less favourable' means, as we have previously said, according conditions of competition no less favourable to the imported product than to the like domestic product."

¹⁸⁸ Para. 53

¹⁸⁹ "Although this requirement does not distinguish between services supplied by service suppliers of Canada and those supplied by service suppliers of other Members present in Canada, it is bound to have a discriminatory effect against services supplied through modes 1 and 2, which are services of other Members." Panel report, *Canada-Autos*, Para 10.307

would apply. In sum, as concluded in *US-Gambling*, the measures would not be justified under Article XIV GATS.

C.5. Conclusion on obstacles to trade

Article 2.1 of the Trade Barriers Regulation defines "obstacles to trade" as "any trade practice adopted or maintained by a third country in respect of which international trade rules establish a right of action. Such a right of action exists when international trade rules either prohibit a practice outright, or give another party affected by the practice a right to seek elimination of the effect of the practice in question."

It has been shown that the US measures under investigation are inconsistent with Articles XVI and XVII of the GATS, and are not justified under Article XIV of the GATS. Since the WTO Agreement prohibits the US measures under investigation, there is evidence of an obstacle to trade in the sense of Article 2.1 of the Trade Barriers Regulation.

D. ADVERSE TRADE EFFECTS

D.1. Introduction

The complainant alleges that the treatment applied by US authorities to foreign operators forced EU Internet gaming companies to withdraw from the US market in October 2006. This had significant adverse effects on the companies affected by the withdrawal. Moreover, the existence of DOJ investigations into EU Internet gaming companies, and the threat of possible future sanctions in the form of substantial fines and convictions, which may include imprisonment of individuals, amount to extreme threats that imply both further additional adverse effects because they prevent the companies to operate their business outside the US under normal conditions, and potential significant adverse effects if those threats were to materialise and sanctions became a reality.

In addition, the complainant alleges that the US measures have a broader impact, both on the EU gaming sector (e.g. by preventing consolidation) and through knock-on effects on those sectors that supply services to the Internet gaming sector. The complaint mentions in particular financial services, IT services, media services, sports sponsorships and professional services in the EU. Furthermore, it points at the possibility that US enforcement actions may spread to those companies as well. It also remarks that DOJ investigations have created a "climate of fear" affecting not only the gaming industry but also a large number of potential targets of DOJ enforcement actions in other sectors that supply services to Internet gaming businesses, including because of the existing extradition treaties of EU Member States with the US.

The Commission services will examine in this section adverse trade effects consisting of the impact of the US measures on EU companies. The analysis will also consider potential adverse effects in the form of opportunities and revenue foregone as a result of the US measures, both for EU companies that had been supplying into the US market and for companies which have never supplied into the US market. A similar analysis will then be conducted with respect to EU companies that supply supporting services to Internet gambling and betting operators. The analysis will then turn to the allegations of threat of adverse effects. Finally, the Commission services will assess whether these adverse trade effects "have a material impact on the economy of the Community or a

region of the Community, or on a sector of economic activity therein" as required by Article 2.4 of the Trade Barriers Regulation.

The Commission services wish to underline that most of the operators that have responded to the questionnaires sent out as part of this investigation, and others that have provided information to the Commission services, have asked the Commission to maintain at least part of the information supplied confidential. Moreover, some of these operators have asked the Commission not to disclose their identity, or even the fact that they have been in contact with the Commission services regarding this investigation.

The Commission services consider that there is a serious risk that any such disclosure could "have a significant adverse affect upon the supplier or the source of such information" in the sense on Article 9.3 of the Trade Barriers Regulation, and will therefore fully respect the confidentiality requested. However, the Commission services will disclose general information that is considered relevant to "justify the reasons on which decisions taken pursuant to this Regulation are based", with full respect "of the legitimate interests of the parties concerned that their business secrets should not be divulged" in the sense of Article 9.5 of the Trade Barriers Regulation.

D.2. Adverse trade effects on remote gambling and betting companies

*[...] provided remote gambling and betting services to customers located in the US at some point before the enactment of the UIGEA. [...] Other EU companies did not offer services in the US as a result of the risks derived from the US legal framework applying to remote gambling and betting services.

EU companies that were present in the US market in the past have explained to the Commission services that they considered their presence in the US market to be legal under US law, and this as a result of several factors:

- The US legal framework applying to remote gambling and betting services was extremely unclear, with differing interpretations as to e.g. the location where an Internet gambling and betting transaction would take place; the sharing of competences between states and the federal level and the implications of the "dormant commerce clause" doctrine; the applicability of key laws to specific types of remote gambling and betting (e.g. sports vs. non-sports; games of skill vs. games of chance);
- The existence of a flourishing local industry supplying remote gambling and betting services;
- The absence of any intervention or communication from the US government to EU regulators (notably UK regulators) with respect to the (obviously widely publicized) listing of EU companies shares on EU stock exchanges. [...]
- The existence of US GATS commitments on the cross-border supply of gambling and betting services.

However, following the enactment of the UIGEA, all EU companies that had been offering remote gambling and betting services into the US withdrew from the market. The enactment of UIGEA certainly played a role in the withdrawal of EU companies from the US market. These companies have explained to the Commission services how the UIGEA, despite its stated objective of not altering what constituted "unlawful Internet gambling", did have an impact on the definition of what could be considered

lawful and unlawful in the US, with the result that, often on the basis of external legal advice, they decided to withdraw from the market. Moreover, the withdrawal was also linked to an intensification of US enforcement actions against foreign operators around the time of the enactment of the UIGEA.

The Commission services have not reached a conclusion on whether the intensification of enforcement actions was a result of the adoption of UIGEA or rather a parallel development where both elements (UIGEA and intensification of enforcement actions) were the result of a single policy drive. In any event, the Commission services consider that there is a clear causal relation between the withdrawal of the companies from the market and both the adoption of UIGEA and the intensification of enforcement actions based on the US legal framework applying to remote gambling and betting services as interpreted by the US authorities. Furthermore, there is also a clear causal link between specific enforcement actions and impact on the business of the companies affected by those enforcement actions. Finally, there is a clear causal link between the US legal framework, including as interpreted by the DOJ and the decision of certain EU companies not to access the US market.

D.2.1. Loss of revenue

The information available to the Commission services shows that the impact of the withdrawal from the US market on the revenues of EU companies was substantial. The annual reports of three EU companies members of the RGA (888.com, PartyGaming, and Sportingbet) that used to provide gambling and betting services remotely into the US contain detailed (and audited) data. The relevant figures for these companies show that their US revenues had been growing strongly until the discontinuation of their US operations in 2006. The revenues obtained from their US operations by these three companies before the impact of the UIGEA started to be felt, reached the following amounts:

US revenues in million \$ (and €)	Last financial year prior to UIGEA¹⁹⁰
Partygaming	824.5 (696.2)
888 Holdings	148 (124.9)
Sportingbet	2,096.5 (1,643.3)
Total	3,069 (2,464.4)

In sum, the direct losses in revenue due to the loss of the US market for just these three companies were above \$3 billion in 2006. These losses are very significant, not only in absolute terms but also in relative terms with respect to the total revenue of the relevant companies (above 50% in the case of Sportingbet and 888 Holdings, and above 80% in the case of Partygaming). Given the evolution of the revenue streams until 2006, one

¹⁹⁰ For Sportingbet, this is the financial year ending 31 July 2006; for Partygaming and 888 Holdings, this is the financial year ending 31 December 2005

could have expected these revenues to continue growing in the following years. Moreover, the companies have indicated that the loss of US revenues implied also the loss of non-US revenues as a result of the reduction of overall "player liquidity" in these companies' websites, which in turn drew players outside the US to competing sites that continued to accept US customers.

Moreover, Bwin lost its US business as a result of the 2006 regulatory changes in the US and its withdrawal from the market. This implied an impairment charge of €515 million in its 2006 accounts, and a revenue loss amounting to €73 million.

D.2.2. Revenue foregone

The complaint by the RGA indicated that EU remote gambling and betting companies had refrained from offering gambling and betting services on horse racing because they considered the Wire Act to prohibit the cross-border supply of this type of gambling. A majority of EU companies focused on non-sports betting because, in their view, there were no US laws that effectively prohibited such gambling.¹⁹¹ Moreover, when discussing the question of "likeness" for the purpose of Article XVII GATS, the complaint also indicated – quoting EC comments as a third party in the *US-Gambling* proceedings referred to above - that "if the competitive relationship is distorted, (or absent) owing to a measure applied in the territory into which the service is being supplied, the relevant benchmark is the potential competitive relationship that would exist if the services supplied were not subject to that measure".¹⁹²

The implication is that, beyond the direct losses as a result of the withdrawal from the US market (which, for each company, imply different segments of the market, depending on the segments where each company had been active), the revenue foregone by EU companies as a result of the US measures is substantial.

Estimating the total amount of revenue foregone would require establishing a "counterfactual" situation.¹⁹³ The Commission services consider that it is not necessary to address this question in detail in this report. However, it should be noted that the issue was addressed in the Article 22.6 of the DSU Arbitration Award in *US-Gambling*,¹⁹⁴ where the arbitrators considered two main alternatives: a counterfactual in which the US would open the US market for remote gambling without restriction, and a partial opening of a limited segment of the market (essentially remote gambling on horse racing). Although the Arbitration Award opted for the "counterfactual" consisting of the partial opening of a limited segment of the market, a dissenting arbitrator did not agree with this view and remarked that it was not unreasonable to assume a counterfactual scenario under which the US would provide unrestricted access to its remote gambling and

¹⁹¹ See complaint by RGA, paras. 58 and 72

¹⁹² Complaint by RGA, para. 71

¹⁹³ Reflecting a situation on gambling and betting services in the US that is fully WTO compliant. This tool is typically used in Article 22.6 DSU arbitration awards as a way of determining the level of nullification or impairment and therefore the amount of compensation due as a result of a Member's failure to bring WTO-inconsistent measures into compliance with the relevant agreements.

¹⁹⁴ Article 22.6 Arbitration Award, *US-Gambling*, paras. 3.16 - 3.73

betting market. Moreover, the dissenting arbitrator pointed at further problematic aspects of the US measures.¹⁹⁵

In any event, it is important to note that this investigation has shown that EU remote gambling and betting operators, including those which have never offered gambling and betting services to US customers, would consider the potential opening of the US remote gambling and betting market as a very valuable business opportunity. One EU remote gambling and betting operator has observed in the context of this investigation that the decision not to offer services to US customers in light of the regulatory uncertainties involved was clearly at a huge commercial expense. Moreover, EU remote gambling and betting companies consider that an approach consisting of opening the market subject to adequate regulation would not only allow the US to collect tax revenue on economic activity that is, in any event, taking place, but also adopt adequate measures - that are obviously not in place at the moment- to protect the consumers.

Although not an Internet gambling and betting company, it is interesting to note that a physical bookmaker operating in the Community and considering international expansion, which heavily relies on telecommunications networks to offer its services, has indicated to the Commission services during this investigation that it considers itself ideally poised as a potential entrant into the US betting market. However, the risks for their business model that derive from the US remote gambling and betting legal environment have led this company to refrain from entering the market. This has implied a loss of major potential markets and income streams, with the added consequence that the absence of the US market inhibits the desired globalisation of the brand.

As an indication of the amounts that might be involved if the remote gambling and betting market was opened – and therefore of the revenue foregone by EU companies -, it is interesting to refer to a study conducted in relation to the introduction before the US Congress on 26 April 2007 by Representative Barney Frank (D-MA) of H.R. 2046, the "Internet Gambling Regulation and Enforcement Act of 2007," that provided for the licensing and regulation of Internet gambling. The purpose of the study was to provide an estimate of the federal revenue that would result from regulating and taxing online gambling, as a result of the existing wagering tax, a newly introduced licensing fee, and individual and corporate income taxes. The study estimated federal revenue to range from \$10.9 billion to \$21.4 billion over the period 2009 – 2018, depending on whether 10 individual states would either allow or continue prohibiting online gambling.¹⁹⁶

Moreover, it should also be noted that there appears to be a thriving online gambling industry that continues to operate on the US market in market segments from which EU companies members of the RGA withdrew following the passage of the UIGEA.¹⁹⁷

The Commission services consider that, without prejudice to the Commission's views on the choice of counterfactual in *US-Gambling*, and the fact that the reasoning in this report is consistent with the alternative of the US opening up its entire remote gambling

¹⁹⁵ Article 22.6 Arbitration Award, *US-Gambling*, paras. 3.62 - 3.65

¹⁹⁶ "Estimate of Federal Revenue Effect of Proposal to Regulate and Tax Online Gambling." Price Waterhouse Coopers. September 26, 2008. Update of the original study of 6 December 2007

¹⁹⁷ See in this respect data on this industry available at <http://www.pokerscout.com/IndustryOverview.aspx>

and betting market subject to adequate regulation, the calculation of the revenue foregone by EU companies requires the assessment of, at least, the value of the market segment consisting of remote wagering on horse racing. This segment was considered by EU companies to be reserved to US based operators, and this fact has been relevant for reaching the conclusion in this report that an obstacle to trade in the sense of the Trade Barriers Regulation exists.

With regard to the segment of horse racing, the volume of wagering on animal racing in the US is about \$20 billion, with about \$15 billion wagered on horse racing only.¹⁹⁸ According to the American Horse Council, remote wagering represents 80% of the total wagering on horse racing in the US.¹⁹⁹ This report provides in section C.3.2 above figures of the amounts wagered on horse racing through the major US suppliers, including for example \$716.0 million through Youbet.com, \$1 billion through NYCOTB or \$175.6 million through ExpressBet.com. It is difficult to anticipate the market share that EU companies could reach if they operated in this segment of the market. Still, taking a conservative approach, it is not unreasonable to assume that EU companies could process wagers at least equivalent to the amounts wagered through NYCOTB. Assuming that their net revenue would be similar to that of NYCOTB, a net revenue of \$125 million per year could be reasonably expected from EU companies if they were to operate in this segment.²⁰⁰

There are further sources of revenue foregone by EU companies. The complaint alleges that the uncertainty created by the US measures affect the ability for EU companies to operate their business under normal conditions. This was argued in particular with respect to the EU companies' access to finance.

This investigation has shown that suppliers of supporting services to the remote gambling and betting industry do indeed refrain from doing business with remote gambling and betting operators. This has implied, for example, difficulties to raise debt and equity finance; freeze of consolidation operations throughout the industry (e.g. termination of the relevant discussions between Ladbrokes and 888 Holdings, or between Bwin and Sportingbet); refusal of investment banks to write equity research on

¹⁹⁸ According to a document by the NTRA, "[P]ari-mutuel wagering is now legal in 43 states, with approximately \$20 billion wagered (or "handled") annually on horses, Greyhounds and the game of jai alai. Three-quarters of all U.S. pari-mutuel handle (\$15 billion) comes from wagering on Thoroughbred racing." ("Improving Security in the US Pari-Mutuel Wagering System: Status Report and Recommendations". The NTRA Wagering Technology Working Group in conjunction with Giuliani Partners LLC. August 2003.) This figure appears to be valid still today (see e.g. press release "Purses up, handle steady in 2007" on NTRA's website at <http://www.ntra.com/content.aspx?type=pr&id=30397>).

¹⁹⁹ "Pari-mutuel wagering on horse racing is licensed and regulated in over forty states. It is wagering, including simulcast wagering and advance deposit wagering, that supports this industry and its underlying agri-business. In the last 25 years interstate wagering, and particularly advance deposit wagering through various forms of electronic media, including the Internet, have grown dramatically. This growth has been pursuant to state law and the Interstate Horseracing Act ("IHA"). Indeed such wagering now represents over 80% of the amount wagered on horse racing in the U.S. For this reason, these forms of wagering, and therefore the proposed regulations, are critical to the racing industry." Comments by the American Horse Council on Comments on the Notice of Joint Proposed Rulemaking Prohibition on Funding of Unlawful Internet Gambling. 12 December 2007.

²⁰⁰ See "New York City Off-Track Betting Corporation. A Plan for Transformation and Growth", p. 6, at <http://www.nycotb.com/newnycotb/Portals/0/downloads/Apr2-07-BostonConsultingGroup.pdf>

the companies, thus reducing their attractiveness to investors, or of accounting and other professional services firms to act as advisers to the companies.

It can therefore be concluded that, as a result of the US measures, EU remote gambling and betting companies forego significant business opportunities also in this respect. The precise amount of revenue foregone as a result of the impact of the US measures on the conditions of operation (which also include other difficulties such as the impact of specific travel policies or management focus on the US measures) is difficult to estimate, but is likely to be significant. A clear proof of how the uncertainty created by the DOJ investigations is affecting the business prospects of EU remote gambling and betting companies is the fact that Partygaming shares went up by more than 27%²⁰¹ on the day of the announcement of Mr Dikshit's settlement with the DOJ.²⁰² Just the prospect of the uncertainty being removed significantly pushes up share prices (including, although less markedly, of other remote gambling and betting companies) reflecting market expectations of improved business prospects in the absence of DOJ enforcement threats.

D.2.3. Loss of stock market value

The information available to the Commission services shows that the impact of the withdrawal from the US market on the stock market value of EU companies was also substantial. Within the period of 9 months shown in the table below three EU companies members of the RGA lost more than 75% of their stock market value, exceeding GBP 5.7 billion (over €8.3 billion, \$11 billion) in losses for these three companies alone.

Evolution of stock market value in GBP (and €) million	Value 31.01.2006	Value 31.10.2006	Total Value loss
PartyGaming	5,130 (7,498)	1,220 (1,821.3)	3,910 (5,676.7)
888 Holdings	681.8 (923.5)	363.2 (542.2)	318.6 (381.3)
Sportingbet	1,749 (2,556.5)	205.5 (306.8)	1,543.5 (2,249.7)
Total	7,560.8 (10,978)	1,788.7 (2,670.3)	5,772.1 (8,307.7)

Moreover, Bwin, a company not member of the RGA, lost in 2006 €120 million in stock market value as a result of its withdrawal from the US market.

²⁰¹ From a price of GBX138.7 to GBX176.5. The price continued to go up in the following days, up to a closing price of GBX211 on 18 December 2008

²⁰² See section C.3.1 above

D.2.4. Liquidation

Betonsports PLC, a publicly traded holding company incorporated in the UK, did business in the United States by offering wagering on sports and sporting events via telephone and the Internet. Betonsports PLC took in wagers amounting to over \$1 billion per year between 2002 and 2004. Following the indictment of the company in June 2006 and its guilty plea in May 2007, the company went into liquidation and no longer operates.

D.3. Adverse trade effects on suppliers of supporting services to remote gambling and betting companies

The Commission services note that EU suppliers of supporting services to EU Internet gambling and betting companies have been particularly cautious in their responses to the questionnaires sent out as part of this investigation. Moreover, the responses and information received provide few concrete figures on the evolution of the business of these suppliers as a result of the US measures.

It is nonetheless obvious that the size of EU suppliers of remote gambling and betting services and the volume that their US operations reached in the past, and the additional fact that several of them are (or were) publicly listed companies, implies a high likelihood of significant adverse effects on the companies supplying services to remote gambling and betting operators as a result of the adverse effects suffered by the remote gambling and betting operators. The Commission services have found evidence of this type of effects in this investigation. Moreover, this investigation has also shown adverse trade effects suffered directly by the suppliers of supporting services themselves.

D.3.1. Loss of revenue and revenue foregone

As indicated above, remote gambling and betting companies have reported difficulties in raising debt and equity finance; a freeze of consolidation operations throughout the industry; the refusal of investment banks to write equity research on the companies, or of accounting and other professional services firms to act as advisers to the companies. The logical implication is that supporting services companies that refrain from providing these services must suffer an adverse effect on their revenue.

EU banks that provided services to remote gambling and betting operators, such as investment and commercial banking services, including corporate finance, broking, research, underwriting and payment processing services, have in the context of this investigation reported a significant decrease in revenues obtained from these services as a result of the US measures. Moreover, they have explained that they have significantly reduced or even stopped activities with remote gambling operators. However, the Commission services have only received generic indications of the amounts that may be involved. These impact indications point in the direction of tens of millions of euros.

IPOs and mergers and acquisitions constitute significant sources of revenue for suppliers of financial and professional services. Any reduction or freeze of activity in a given sector can impact the suppliers of these supporting services. The Commission services have therefore considered the IPOs of some of the relevant EU companies offering remote gambling and betting companies. Although IPOs are one-off events, the Commission services consider that they can provide a useful indication of the amounts that may be involved in the supply of supporting services to these companies.

In this respect, the IPO of Partygaming in 2005 constituted the third largest IPO of the year, raising €1.4 billion.²⁰³ Although the costs of raising equity decline in proportion to the size of the issue, and specific companies can therefore incur costs that are very different from the overall costs observed on the market, the average underwriting fee in European markets is 3-4% of the amount issued. Legal, accounting and advisory fees can add a further 3-6%.²⁰⁴ The closure of the US market as a result of the US measures has undoubtedly acted as a brake on the development of the remote gambling and betting sector, and must have had an impact in this respect.

Mergers and acquisitions are a source of significant income for banks and other suppliers acting as advisors. Although information on the fees charged by the relevant advisors is not easily available, it appears safe to assume that the total fees paid to advisors in any merger or acquisition would not be below 1 % of the total transaction value.²⁰⁵ The consolidation operations that were being considered and then failed as a result of the US measures (Ladbrokes and 888 Holdings; Sportingbet and Bwin) would thus have represented a very significant amount in fees for the relevant suppliers of supporting services to remote gambling and betting companies.

Firms acting as legal advisors to the remote gambling and betting industry also suffer adverse effects from the US measures. A law firm providing legal advice to remote gambling and betting operators has indicated that its revenues from this source are in excess of \$10 million per year. This firm cannot provide a precise figure of the revenue foregone as a result of the US measures, but indicates that they would have expected to play a significant advisory role in the significant transactional activity that would have taken place in the absence of US enforcement measures. Moreover, they consider these measures to have stifled development and consolidation in the sector.

Payment processors other than banks have also suffered and continue to suffer the impact of the US measures. As indicated above, US enforcement actions have targeted payment processors directly. Indeed, Neteller announced on 18 July 2007 that it had admitted DOJ charges of criminal conduct and the forfeiture of \$136 million. Ireland-based FireOne Group plc, a then majority-owned subsidiary of the Canadian company Optimal Group, ceased to process settlement transactions originating from United States consumers related to online gambling as a result of the passage of the UIGEA. Optimal group reported that the withdrawal from the US market had and would continue to have a significant negative impact on the financial results of FireOne Group plc. Such transactions represented more than 80 % of FireOne's total revenue. The prospect that FireOne might not be able to identify and engage in other opportunities that would offset

²⁰³ See "IPO Watch Europe. Review of the Year 2005", Price Waterhouse Coopers, at http://www.pwc.co.uk/pdf/ipo_watch_review_2005.pdf

²⁰⁴ See "The Cost of Capital: an International Comparison", London Stock Exchange and Oxera, at <http://www.londonstockexchange.com/NR/exeres/E9A703D2-6818-4A60-9C23-7DA9FBD0BB4D.htm>

²⁰⁵ Sellers usually pay M&A fees that are a percentage of the total transaction value. The relevant fee will sometimes include a minimum fee, or be composed of a fixed and a variable element. A 2002 study conducted by William C. Hunter of the Federal Reserve Bank of Chicago and Julapa Jagtiani of the Federal Reserve Bank of Kansas City entitled "An Analysis of Advisor Choice, Fees and Effort in Mergers and Acquisitions" and analysing empirical evidence concluded that "[O]n average, total fees (paid by both targets and acquirers) were 1.22 percent of the transaction value" (p.4). Available at http://www.kansascityfed.org/Banking/BankingPublications/2002_RFE_SpecialIssue.pdf

the lost revenue implied that FireOne had to restructure its operations and cost base, at a cost estimated at \$1.5 million. Given that its future as an independent listed entity was considered uncertain, Optimal Group acquired all of its shares in order to combine its operations with those of its subsidiary Optimal Payments UK.²⁰⁶ UC Group, a UK based payment processor, has also reported adverse effects from the US measures. It has informed the Commission that its decision not to do business with online gambling firms with US activities either before or after the passage of the UIGEA implied a foregone revenue in excess of 60% of the processing volumes that would otherwise have been available to the company, and more than 50% in revenue in some months. The UC Group maintains in information supplied to the Commission services that foregone income would have been around \$300 million in the period 2005 – 2006.

D.4. Adverse effects on specific regions of the Community

Malta is a principal jurisdiction for the establishment and regulation of remote gaming companies within the EU. Malta's government has indicated to the Commission services that it has invested significantly in the development of a sound regulatory regime and supporting service industries and infrastructures. As a result, the gaming sector forms a recognised source of direct and indirect job creation within the Islands' increasingly service oriented economy. The government of Malta estimates that in 2007 Malta had a 12% share of the world online gambling market,²⁰⁷ which contributed to over 5% of Malta's GDP and over 6% of the gross value added of the Maltese Economy. Moreover, as indicated in section B.1.1 above, the remote gambling and betting industry had 1,882 direct employees in Malta in 2008.

US measures that prevent access to a market which represents approximately 50% of the global market bears an actual and potentially significant impact on the gaming companies that are established in Malta and which trade internationally on a direct and indirect basis. Maltese authorities have noticed variations in the financial stability and performance of the remote gambling and betting companies which have required direct regulatory intervention on the Malta-based operations. Moreover, the more recent US measures have slowed down and even stopped these companies' investment and growth plans due to the uncertainty that persists in the market. While the quantum of this negative impact may not be easily calculated, it is considered obvious that the growth potential of the sector has been severely affected and that the investments made in supporting infrastructures may indeed be stranded.

According to a study provided to the European Commission in the context of this investigation,²⁰⁸ the online gaming industry accounts for 10% of Gibraltar's GDP and employs directly more than 8% of total employment (1,689 jobs), which rises to 18.2% if indirect employment is considered (a further 2,548 indirect jobs). The study further indicates that as a result of the UIGEA, there was a loss of income equivalent to 10% (£50.8) of the total wages, salaries and profits paid throughout the Gibraltar economy in

²⁰⁶ See in particular "Recommended Cash Offer by Optimal Acquisition Inc for FireOne Group plc" at http://www.fireonegroup.ie/press_releases/FireOne_Offer.pdf

²⁰⁷ Estimated by Malta at \$15 billion in 2006

²⁰⁸ "The Economic Impact of the Introduction in the US of the Unlawful Internet Gambling Enforcement Act on the Online Gaming Industry of Gibraltar." Report on behalf of Hassans International Law Firm by Professor John Fletcher

2006, a loss of government revenue of 8% (£ 19.5 million) and a loss of total jobs of 7.3% (1,359 jobs).

The Commission services consider that the effects on Malta and Gibraltar described in this section qualify as "adverse trade effects" within the meaning of the Trade Barriers Regulation.

D.5. Threat of adverse trade effects

The complaint referred to the possible sanctions that may be imposed on EU suppliers of remote gambling services as a result of ongoing DOJ investigations. These possible sanctions could include payments of substantial fines, convictions of the companies and imprisonment of individuals. They were described as "extreme threats" by the complainant. Moreover, the complaint argued that if the potential sanctions were to become a reality, the impact on the companies would be significant and would seriously affect the ability of the companies to compete in any market. Moreover, the complaint referred also to the concerns of the financial industry that they could become a target of enforcement actions because of their work for Internet gaming companies.²⁰⁹

The Commission services inquired as part of the investigation about pending and possible future DOJ investigations, but did not receive any information from the US government. The US government explained in this respect to the Commission services that the DOJ does not make public comments on pending and possible future investigations prior to the initiation of judicial proceedings.

The Commission services consider that the experience of past and ongoing investigations regarding EU remote gambling and betting suppliers, as well as regarding suppliers of supporting services to EU remote gambling and betting suppliers, is sufficient to conclude that a scenario in which current investigations develop into actual and additional serious adverse trade effects is clearly foreseeable. The seriousness of the threat and the importance of the potential adverse effects are evident based on the examples of enforcement action described above.²¹⁰

The Commission services further consider that additional EU remote gambling and betting suppliers and the relevant supporting services suppliers may become the target of future DOJ investigations. What is more, the Commission services do not exclude that investigations against EU suppliers in addition to those identified in this report may be already taking place. However, the affected EU suppliers may have opted for not informing the Commission services of the existence of such investigations in order to avoid any risk of disclosure. The extreme caution of many EU suppliers with which the Commission services have been confronted in the course of this investigation is in itself a signal of both the seriousness of the threat and of the real concern of EU suppliers that a situation of involvement with online gambling offered to US customers may develop into DOJ investigations and/or serious criminal sanctions.

²⁰⁹ Complaint by RGA, paras. 107 to 109, para. 114.

²¹⁰ The cases of Neteller and Mr Anurag Dikshit, founder of Partygaming, are particularly telling in this respect. Partygaming itself announced on 16 december that they are working towards a settlement with the DOJ

D.6. Material impact

Article 2.4 of the Trade Barriers Regulation requires the existence of "a material impact on the economy of the Community, or of a region of the Community, or of a sector of economic activity therein." Article 10.4 of the Trade Barriers Regulation provides that in examining such impact, the Commission shall take account, where relevant, of factors of the type listed in paragraphs 1 and 2 of Article 10. It further adds that adverse trade effects may arise, *inter alia*, in situations in which trade flows concerning a product or service are prevented, impeded or diverted as a result of any obstacle to trade, or from situations in which obstacles to trade have materially affected the supply of inputs to Community enterprises. Moreover, where a threat of adverse trade effects is alleged, the Commission shall also examine whether it is clearly foreseeable that a particular situation is likely to develop into actual adverse trade effects. Finally, Article 10.6 indicates that the list of factors and the indications given in paragraphs 1 to 5 of Article 10 are not exhaustive, and that neither the existence of one nor of several of the factors and indications must necessarily imply that adverse trade effects exist.

As shown in the above analysis, and as a result of the obstacle to trade, EU enterprises have suffered very significant revenue losses and a very significant decrease of market capitalisation; have foregone and continue to forego very significant amounts of potential trade and revenue; and are in a situation which is clearly foreseeable that is likely to develop into actual additional adverse trade effects. Affected EU enterprises are to be found both in the gambling and betting sector, and in services sectors providing services to the gambling and betting industry, notably financial and professional services.

Moreover, as a result of the obstacle to trade, Malta has suffered a non quantified but significant negative impact on its economic activity and employment. Gibraltar has suffered a quantified and significant negative impact on its economic activity and employment as well.

EU remote gambling and betting enterprises affected by the obstacle to trade are important players in the EU gambling and betting sector. Although online gambling and betting still only represents around 4% of the gambling and betting sector in the EU, the size of the enterprises affected is substantial and the volume of their operations is very substantial, as shown by the hundreds of millions of euro in revenue that they collect every year.²¹¹ The investigation has also shown that important EU enterprises supplying supporting services to the gambling and betting industry, notably in the financial and professional services sectors, have also been significantly affected.

On the basis of the above considerations, the Commission services consider that the adverse trade effects described in the preceding paragraphs have a material impact on the sector of gambling and betting services in the Community, on the sector of financial

²¹¹ As indicated in section B above, in 2007, Ladbrokes had a total operating income of £1.2 billion (almost €1.4 billion at 2008 rates) and a market capitalisation of £1.9 billion (€2.2 billion); William Hill had a total revenue of £940 million (more than €1 billion) and a market capitalisation of around £2 billion (€2.2 billion); Sportingbet had a total operating income of £119.4 million (€133 million) and a market capitalisation of £221.9 million (€247.6 million); Paddy Power had a total operating income of €278.9 million and a market capitalisation of €1.1 billion; Bwin had total revenues of €336.9 million and a market capitalisation of €650.96. These figures correspond to all the operations of the relevant companies, including where appropriate non-online operations.

services, and on the sector of professional services. Moreover, the Commission services consider that the adverse effects described in the preceding paragraphs have a material impact on regions of the Community.

D.7. Conclusion

The Commission services conclude that the obstacles to trade cause adverse trade effects to the complainant and to EU enterprises that are not members of the complainant, which have a material impact on a sector of economic activity and on a region of the Community. Therefore, the Commission services consider that the obstacles to trade cause adverse trade effects within the meaning of Article 2.4 of the Trade Barrier Regulation.

E. COMMUNITY INTEREST

The Trade Barriers Regulation provides no definition of the “interests of the Community”, any more than it states the rules governing the examination of those interests. The Court of First Instance has confirmed that the Commission enjoys a wide margin of discretion in assessing Community interest under the Trade Barriers Regulation. In its understanding of Community interest, the Commission is guided by the following provisions of the Trade Barriers Regulation referring to Community interest:

Article 8(1) provides that the Commission is to initiate an examination procedure “where, after consultation, it is apparent to [it] that there is sufficient evidence to justify initiating an examination procedure and that it is necessary in the interest of the Community”. Article 11(1) of the Trade Barriers Regulation states that “when it is found as a result of the examination procedure that the interests of the Community do not require any action to be taken, the procedure shall be terminated in accordance with Article 14”. Article 12(1) provides that “where it is found (as a result of the examination procedure, unless the factual and legal situation is such that an examination procedure may not be required) that action is necessary in the interests of the Community in order to ensure the exercise of the Community’s rights under international trade rules, with a view to removing ... the adverse trade effects resulting from obstacles to trade adopted or maintained by third countries, the appropriate measures shall be determined”.

The Commission also considers relevant the 15th recital in the preamble to the Trade Barriers Regulation, which states that “it is incumbent on the Commission ... to act in respect of obstacles to trade adopted or maintained by third countries, within the framework of the Community’s international rights and obligations, only when the interests of the Community call for intervention, and ... when assessing such interests, the Commission ... should give due consideration to the views [of] all interested parties in the proceedings”.

In line with this understanding of Community interest under the Trade Barriers Regulation, and as shown by the analysis in section B of this report, it has to be noted that the EU has developed the world's leading remote gaming business. Many of the world's largest companies are licensed in and operate from the UK, Gibraltar, Malta, Ireland and Austria. There are significant back office operations providing technology, marketing and customer service support in other Member States. Although accurate statistics on this sector are not readily available, the sector is economically significant, with an estimate of more than 10,000 staff employed by the remote gaming industry in

the EU. Moreover, this sector has a significant indirect economic impact on other sectors of the economy which are involved in providing the infrastructure that this type of business requires (primarily financial services, information technology and professional services).

European Lotteries submitted that RGA did not initiate the proceedings in an attempt to remedy the obstacle to trade which exists within the US. The US has already initiated lawfully the procedure to withdraw its commitments in the sector of gambling services. According to European Lotteries, the only commitments the US has to maintain concern horse racing. For European Lotteries, this shows that the procedure does not seek the removal, nor will it have as its outcome the removal of the alleged obstacles to trade on the export market. European Lotteries identifies as only reason for RGA to initiate these procedures the fact that a number of its members are being prosecuted in the US. European Lotteries concludes that RGA is trying to divert the purpose of the Trade Barriers Regulation to make up for the impossibility it faces of invoking the rules of the WTO. Accordingly, an action in this case could not be considered to be in the interest of the Community, as taking further steps would result in undermining the ECJ's judgements in the Van Parys case, and would open the door for other private parties to invoke the decisions of the WTO in a diverted manner, through the Commission's Trade Barriers Regulation procedure.

This argument has three lines. The first one is concerned with what particular outcome may result from this procedure, and whether removal of the obstacles to trade may be achieved. The second line of argument relates to the motivation of RGA, and an alleged attempt to "divert the purpose of the TBR". The third line concerns the ECJ's judgment in the Van Parys case.

Concerning the first line of argument, this speculative assessment of how the US might react does not outweigh the Community's important systemic concern to defend the WTO rights which it negotiated. Moreover, it results from the analysis in section C above that it is by no means a settled issue, as European Lotteries argue, that the only commitments that the US would have to maintain if a successful case was brought concern horse racing. With regard to the second line of argument, RGA has made the case that US laws prohibiting the cross-border supply of remote gambling and betting services as well as their enforcement against Community companies are in violation of WTO law and have caused adverse trade effects. It is not apparent that RGA, in bringing this Trade Barriers Regulation case, was guided by additional motivation that would amount to an abuse of the Trade Barriers Regulation procedure. Regarding the third line of argument, the Trade Barriers Regulation does not lead to giving WTO law direct effect, and it cannot be seen how this application of the Trade Barriers Regulation procedure should undermine the Court's reasoning in the Van Parys case. It is the lack of direct effect of WTO obligations in the US which made it necessary for RGA to request from the EC, through the framework of the Trade Barriers Regulation, action against a WTO breach in the US. It is precisely the purpose of the Trade Barriers Regulation, and of the WTO dispute settlement system, to make up for deficiencies in terms of WTO-compliance in other WTO Members.

European Lotteries submitted further that the Commission must take into account the interests of all companies affected, and that Community action would be contrary to the interests of the major proportion of the industry. According to European Lotteries, taking action against the United States would critically and seriously affect the interests of the companies and Member States it represents.

Leaving divergent economic interests of the various actors in this sector aside, it has to be borne in mind that different parts of the Community industry should in principle compete with one another without the interference of WTO-inconsistent distortions. The economic considerations relating to other actors in the sector do not outweigh the interests of the Community that favour taking action.

The Commission services are aware of the important public policy concerns involved in the area of gambling and betting services, and recall in this sense recital four of the preamble of the GATS, recognizing the right of Members to regulate, and to introduce new regulations, on the supply of services within their territories in order to meet national policy objectives. The WTO Agreement, and the GATS in particular, provide Members with the necessary flexibility to pursue the relevant policy objectives. It is however essential that WTO Members pursue their policy objectives with full respect of their international obligations

The Global Europe Communication from October 2006 calls for activism in creating open markets and fair conditions for trade abroad. Its Action Plan for EU External Competitiveness provides for a renewed Market Access Strategy to help enforce multilateral and bilateral trade deals and open third country markets. In this context, it is important to ensure that other WTO Members, and in particular the US, observe international trade rules, and the obligations contained in the WTO Agreement.

It can therefore be concluded that it is in the interest of the Community to act in respect of the obstacles to trade identified in this investigation.

F. CONCLUSION

The evidence available to the Commission services leads to the conclusion that US laws prohibiting the cross-border supply of remote gambling and betting services as well as their enforcement against Community companies are in violation of Articles XVI and XVII of the GATS, and are not justified under Article XIV of the GATS. As a consequence, the Commission services consider that the investigation has established the existence of an obstacle to trade in the sense of Article 2.1 of the Trade Barriers Regulation.

The Commission services have also examined the effects of the obstacle to trade and have determined that adverse effects within the meaning of Article 2.4 of the Trade Barriers Regulation exist and have been caused by the obstacles to trade identified.

In the light of the foregoing, the Commission services conclude that action is necessary in the interests of the Community.

It should nonetheless be noted that the subsequent steps in this Trade Barriers Regulation procedure would need to take account of the state of play in the ongoing process towards the withdrawal of the US GATS commitments on gambling and betting services addressed in detail in section C.4.2 above, especially given that the definition of the measures at issue and the remedy reasonably available to the EC under WTO rules would be affected by the withdrawal. Moreover, the approach that the new US Administration takes with regard to the subject matter under investigation in this Trade Barriers Regulation examination may also be relevant for determining which subsequent acts are in the interest of the Community. In this respect, the Commission notes that pursuant to Article 11(2) of the Trade Barriers Regulation, when, "after an examination

procedure, the third country or countries concerned take(s) measures which are considered satisfactory, and therefore no action by the Community is required, the procedure may be suspended in accordance with the provisions of Article 14." Also, pursuant to Article 11(3) of the Trade Barriers Regulation, "[W]here, either after an examination procedure, or at any time before, during and after an international dispute settlement procedure, it appears that the most appropriate means to resolve a dispute arising from an obstacle to trade in the conclusion of an agreement with the third country or countries concerned...the procedure shall be suspended according to the provisions of Article 14..."

ANNEX 1

LIST OF MEMBERS – REMOTE GAMBLING ASSOCIATION

Barcrest Ltd

Bellfruit Ltd

Bet 365

Betfair

Blue Square (Rank Group)

Cantor Index

Cashcade

Chartwell Games

CryptoLogic

Eurogaming

Gala/Coral Group

Inspired Broadcast Networks Limited

Ladbrokes

Leisure & Gaming

Littlewoods Gaming

Microgaming

Million 21

Orbis Technology Ltd

Paddy Power

PartyGaming

PKR Ltd

Playtech

Ritz Ltd

Skybet

Sportingbet

Stan James

Stanley

Talarius

Totesport

Unibet

Victor Chandler

Virgin Games

William Hill

32 Red

888.Com