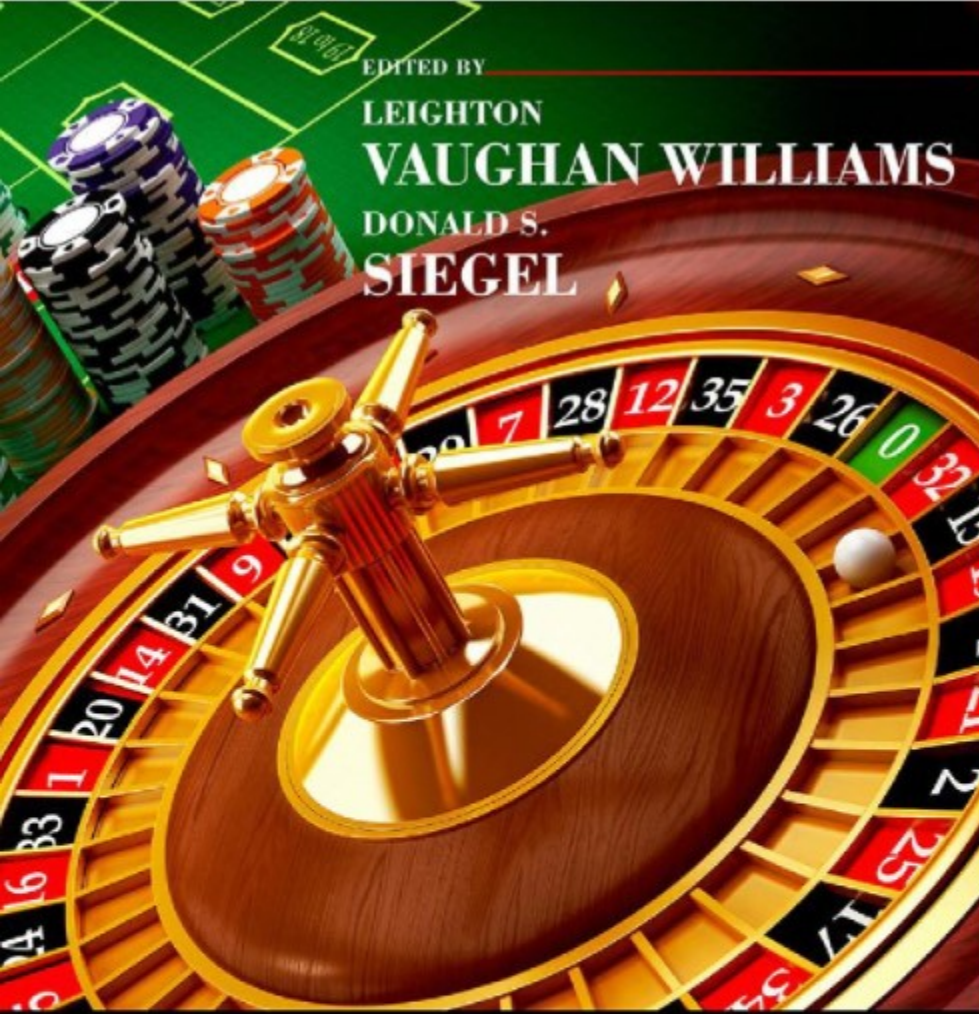




EDITED BY

LEIGHTON

VAUGHAN WILLIAMS

DONALD S.

SIEGEL

III The Oxford Handbook of
**THE ECONOMICS
OF GAMBLING**

Copyrighted material

THE OXFORD HANDBOOK OF

THE ECONOMICS OF GAMBLING

Edited by
LEIGHTON VAUGHAN WILLIAMS
and
DONALD S. SIEGEL

OXFORD
UNIVERSITY PRESS

Copyrighted material

OXFORD
UNIVERSITY PRESS

Oxford University Press is a department of the University of Oxford.
It furthers the University's objective of excellence in research, scholarship,
and education by publishing worldwide.

Oxford New York
Auckland Cape Town Dar es Salaam Hong Kong Karachi
Kuala Lumpur Madrid Melbourne Mexico City Nairobi
New Delhi Shanghai Taipei Toronto

With offices in
Argentina Austria Brazil Chile Czech Republic France Greece
Guatemala Hungary Italy Japan Poland Portugal Singapore
South Korea Switzerland Thailand Turkey Ukraine Vietnam

Oxford is a registered trademark of Oxford University Press
in the UK and certain other countries.

Published in the United States of America by
Oxford University Press
198 Madison Avenue, New York, NY 10016

© Oxford University Press 2013

All rights reserved. No part of this publication may be reproduced, stored in a
retrieval system, or transmitted, in any form or by any means, without the prior
permission in writing of Oxford University Press, or as expressly permitted by law,
by license, or under terms agreed with the appropriate reproduction rights organization.
Inquiries concerning reproduction outside the scope of the above should be sent to the Rights
Department, Oxford University Press, at the address above.

You must not circulate this work in any other form
and you must impose this same condition on any acquirer.

Library of Congress Cataloging-in-Publication Data
Vaughan Williams, Leighton.
The Oxford handbook of the economics of gambling/Leighton Vaughan Williams
and Donald S. Siegel.

pages cm. — (Oxford handbooks)

Includes bibliographical references and index.

ISBN 978-0-19-979791-2 (cloth: alk. paper)

1. Gambling. 2. Gambling—Economic aspects. I. Siegel, Donald S., 1959– II. Title.
HV6710.V38 2013
338.47795—dc23
2012038792

1 3 5 7 9 8 6 4 2
Printed in the United States of America
on acid-free paper

Copyrighted material

SECTION II

SPORTS BETTING

Copyrighted material

CHAPTER 7

THE ECONOMICS OF ONLINE SPORTS BETTING

GEORGE DIEMER AND RYAN M. RODENBERG

I INTRODUCTION

THE technological shock ushered in by the Internet has brought about significant structural changes in many industries. The sportsbook industry is one such example. Michael Smith and Leighton Vaughan Williams (2008, 404) have concluded that it is “now widely accepted that the technologies associated with the internet have spawned radical new business models and formats [and a]spects of the gambling industry are being transformed by these pervasive technologies.” More pointedly, Mark Davies et al. (2005) have explained how five distinct technological forces have revolutionized sports wagering—(1) Moore’s Law pertaining to computing power, (2) Metcalfe’s Law regarding networks, (3) decreased transaction costs as explained by the Coase Theorem, (4) increased potential for customer clustering (also known as the “flock of birds phenomenon”), and (5) diminished barriers to entry via the so-called “fish tank phenomenon.” The technology-induced boom in Internet sports gambling has, in turn, rendered the somewhat antiquated laws “virtually unenforceable” (Cabot and Faiss 2002, 2).

The pre-Internet economic and legal environment of sports wagering was relatively clear, as the industry was heavily concentrated. In this previous era, with full-scale wagering on sports illegal in 49 out of 50 states in the United States,¹ American gamblers had only two options: (1) they could travel to Nevada and gamble on sports legally (at what are known as “terrestrial” gambling sites) or (2) they could place illegal wagers with their local bookie. In the post-Internet age, however, the legal and economic issues involved in sports gambling are much more complex and uncertain. The sports gambling sector has changed dramatically from an oligopolistic to a monopolistically competitive industry unhampered by geography. The geographical sportsbook market

Copyrighted material

was local in nature. The Internet changed that market to a global one. Although there have been sporadic legislative attempts to regulate and/or prosecute the industry in the United States, the legality of the sports gambling industry is currently in a state of flux.

The purpose of this chapter is to provide an overview of the online sports betting industry from an economic and a legal perspective. Our dual focus is one of necessity, as the overlapping, and sometimes conflicting, regulatory environment lends itself to a decidedly “law and economics” inquiry. After an overview of the pre-Internet environment, we proceed to a multifaceted treatment of the online sportsbook, explaining the decided shift in its economic characteristics and the ambiguous legal status in which the industry resides. For the avoidance of doubt, our economic-based coverage is applicable globally. In contrast, the accompanying legal discussion will focus primarily on jurisprudence in the United States, a nation that holds the somewhat ironic distinction of being the world’s largest single-nation sports gambling market and the only major industrial jurisdiction whose laws leave bettors and gambling-related businesses in a legal grey area regarding the permissibility of sports wagering activities.

II PRE-INTERNET LEGAL AND ECONOMIC ENVIRONMENT

The pre-Internet legal and economic environment for sports gambling was highly regulated and heavily concentrated among a few key businesses and locations. It was dominated by terrestrial gambling sites and illegal sportsbooks, both of which operated within relatively stable geographical and legal constraints. While the operations of the illegal sportsbooks are largely clandestine with a few exceptions (Strumpf 2003), the licensed terrestrial gambling sites “present significant opportunities for economic analysis” (Sauer 1998, 2021).

A Terrestrial Sports Gambling Sites

Terrestrial gambling sites, such as the legal sportsbook casinos in Las Vegas and other locations in Nevada, operate in an oligopolistic industry shaped by large barriers to entry. Significant start-up costs, regulatory licenses, and a heavy tax rate serve as barriers to entry into the industry and result in a limited number of competitors in the highly regulated jurisdiction. This may be changing, however. First, Cantor Fitzgerald, a well-known Wall Street firm, has recently made inroads into the Vegas-based sportsbook industry through its subsidiary affiliate Cantor Gaming, operating the upscale M Resort and licensing its real-time “Inside Wagers” technology to a handful of other sportsbooks around Las Vegas. Second, William Hill, a prominent British bookmaking firm,

Copyrighted material

announced the 2011 acquisitions of Nevada-based sportsbooks American Wagering, Club Cal Neva Satellite Race and Sportsbook Division, and Brandywine Bookmaking LLC.

As is the case with most oligopolistic industries, these firms can earn an excessive economic profit. Terrestrial sports gambling sites use a traditional fee, known as vigorish, of 10 percent on all losses. This fee is often thought of as a commission. Traditional literature assumes that the objective of a sportsbook is to balance the action or amount wagered on each side of the game or event. If this objective is attained, the sportsbook takes no risk on the game, as sportsbooks are neutral regarding the actual outcome of the game or event, collect all losing bets (plus the 10 percent vigorish), and pay out the winning bets. This leaves the sportsbook with commission revenue of 5 percent of all action.² Terrestrial sportsbooks are often content with this commission, especially when it brings in additional action to the table games on-site. In addition to traditional wagers, most sportsbooks offer a limited number of so-called exotic wagers similar in form to the pari-mutuel system used by a racetrack to handle its gambling. These systems take in 14 to 20 percent before distributing the winnings (Davies et al. 2005).

B Local Bookies

Prior to the 1840s, most gambling in the United States was heavily rigged and consisted of poker games that took place on steamboats. Gambling was disorganized and decentralized, but this all changed with the construction of major horseracing tracks, such as Saratoga in 1864 and Churchill Downs in 1875. In the 1870s racetracks began introducing Paris Mutual (or pari-mutuel) betting. Pari-mutuel wagering is a type of bet in which the payout odds are tabulated after the race has completed. These odds are a function of where the money was wagered and in what amounts. Updated odds give the gamblers an idea of the expected payout. This type of wager took time to gain popularity but remains the dominant type of racetrack wager today.

Peter Reuter (1983) estimated that the illegal sportsbook industry in New York City's four-firm concentration ratio was no more than 35 percent. He concluded that bookmaker operations were relatively small, with frequent entry barriers but almost no exit barriers. Reuter also found that efforts toward collusion often failed and that the market seemed to operate competitively. However, one signal of monopoly power in the industry still existed—third-degree price discrimination. Koleman Strumpf (2003) found evidence of such third-degree price discrimination within the illegal sportsbook industry. Using a unique data set provided by a county district attorney following several high-profile arrests, Strumpf reached this conclusion by examining six bookmakers who operated in and around the New York City area in the 1990s. Strumpf described the client differentiation that is required in such activity as being relatively easy. Simply by moving the point spread of the local team to make it more expensive to bet on them,

Copyrighted material

the local sportsbooks discriminate against the local geographical bias of the fan base in that area.

C Sportsbook Corruption Pre-Internet

The industry of the racetrack bookmaker relied on an information network just at a time when communication technology was evolving. Bettors with results of prior races that were allowed to wager on off-track locations opened the door for “past-posts.” Exploiting information gaps became a lucrative business for professional gamblers. Filling any existing information gaps became a great concern for bookmakers as they used the services of Western Union for up-to-date information. Federal authorities opted against cracking down on legal or illegal gamblers at these early racetracks, largely so that they could go after affiliated services provided by legally operating businesses like Western Union. By pressuring companies that contributed to illegal gambling, the government sought to indirectly curb the bookmaking business, a trend that continues today.³ Finally, in 1904 Western Union announced it would end the collection and dissemination of race results. This move resulted in large profits for illegal wire transfers companies that practiced price discrimination in connection with the information.⁴

From 1950 to 1951, the U.S. Senate, the nation’s most powerful legislative body, conducted what was officially called the Senate Special Committee to Investigate Crime in Interstate Commerce and commonly referred to as the Kefauver Committee (U.S. Congress 1951). The primary objective of this committee was to investigate organized crime. The investigation led to the conclusion that illicit bookmaking resulted in illegal monopolization of racing information and, in turn, police corruption. This finding put a spotlight on the link between organized crime and bookmaking and served as the impetus for the Wire Act of 1961 (Wire Act), one of the most prominent federal anti-gambling statutes.

The National Gambling Impact Study Commission (NGISC) was authorized by Congress in 1996 and completed its work in 1999 (NGISC 1999). Except for tribal and Internet gambling, the NGISC recommended that gambling be given statewide autonomy. Furthermore, the NGISC advised curtailing statewide lotteries, especially to the extent that they target lower income neighborhoods. The NGISC recommended that collegiate and other amateur sports gambling be reduced or eliminated, a recommendation that was not enacted as legislation at the federal level.⁵

The illegal bookmaking industry changed in many ways between the Kefauver Committee and the time the NGISC was commissioned. What was once dominated by horse races slowly began moving toward what is now known as traditional sports betting. Information gaps were no longer problematic for bookmakers, as transmitting information about the games by broadcasters was acceptable. In addition, with the popularity of the point spread system, taking bets became simpler with fewer events

Copyrighted material

and only two possible outcomes to wager on. Finally, terminology began to change with legitimate bookmaking rings being known as sports books.

III POST-INTERNET LEGAL AND ECONOMIC ENVIRONMENT

Defining the geographical and legal markets for Internet sportsbooks is a complex task. Since its enactment, the Wire Act has prohibited gamblers and bookies from making transactions across state lines over telephone wires.⁶ As such, to steer clear of the statute, bettors and bookies had to be in the same place at the same time. Today, however, there are up to three locations for gambling activity: (1) a domain name registered location, (2) a place of business operation, and (3) a target market where individual gamblers reside. One marketplace often covers multiple geographical locations. As Mark Wilson (2003, 1246) explained: "An example of online gambling is Casino Australia, which has a name suggesting Australia, a domain name registered in New Hampshire in the United States, and a website based in the Netherlands Antilles."

The example of Casino Australia is illustrative of how uncertain the legal environment has become, notwithstanding the fact that a number of Internet sports books are publicly traded in well-respected stock exchanges, such as the London Stock Exchange. In these cases, it is hard to initially identify which nation is responsible for enforcing which nation's gambling laws. Given the reactive nature of lawmaking, statutes and code are just now being codified with Internet-based transactions in mind. For example, on August 7, 2007, after several court rulings had chipped away at the law, the U.S. Congress amended the Foreign Intelligence Surveillance Act of 1978 (FISA) to better fight terrorism. This update allows American investigative bodies to use modern technology in a more expansive way.⁷ It is conceivable that a similar update to the Wire Act could be forthcoming in the not too distant future.⁸ Subsequent interpretations of FISA, the Wire Act, and similarly situated laws enacted before the emergence of the Internet will shape the industry moving forward.

In their examination of international legal regulations in the Internet age, Stephan Wilske and Teresa Schiller (1997) set forth several legal principles for regulating Internet activity within and across national borders. The first and most relevant to Internet gambling is the territoriality principle, which states that a nation has authority over locally produced Web content. This effectively grants a nation the power to have laws restricting Internet businesses from offering services to its citizens, even if the business operates within the nation's borders and provides the services of foreigners legally. A business can comply with such laws by identifying the geographic location of potential customers through their Internet addresses. This practice is common in the Internet sports industry. For example, Australia allows local online gambling sites to operate provided no Australian citizens are allowed to gamble

Copyrighted material

on their sites. In the United States, the territoriality principle is unevenly applied. As a result, many Internet sportsbooks have decided to restrict access to American customers.⁹

A considerable portion of the aforementioned NGISC centered on the then-novel type of gambling that appeared on the landscape—Internet gambling. In its recommendations, the NGISC report concluded:

The Commission recommends to the President, Congress, and the Department of Justice (DOJ) that the federal government should prohibit, without allowing new exemptions or the expansion of existing federal exemptions to other jurisdictions, internet gambling not already authorized within the United States or among parties in the United States and any foreign jurisdiction. Further, the Commission recommends that the President and Congress direct the DOJ to develop enforcement strategies that include, but are not limited to, internet service providers, credit card providers,¹⁰ money transfer agencies, makers of wireless communications systems, and others who intentionally or unintentionally facilitate internet gambling transactions. Because it crosses state lines, it is difficult for states to adequately monitor and regulate such gambling.¹¹

Related NGISC findings included a call for passage of legislation that would curb or prohibit wire transfers involving gambling websites and a recommendation to the president and Congress to facilitate cooperation with foreign governments.

As for the economic environment, the industry appears to be in transition. The post-Internet era of sportsbooks is one that is not oligopolistic or localized. Instead, it is highly monopolistically competitive with a global marketplace. Complicating matters are two non-American judicial proceedings with far-reaching free trade and consumer protection implications—the European Court of Justice's *Liga Portuguesa* decision in 2009 and the 2003 World Trade Organization's *Antigua and Barbuda v. United States* case.¹² The multi-jurisdictional nature of these disputes, coupled with the now monopolistically competitive nature of the industry, suggest an uncertain and likely litigious future.

A Entry Barriers

In the post-Internet era, there are few significant entry barriers in this industry. Starting up a no-frills Internet sportsbook costs approximately ten thousand U.S. dollars, which is used to handle such tasks as acquiring domain names, obtaining the use of servers and phone lines, purchasing or licensing gambling software, and advertising. By operating in Internet-friendly nations (such as Antigua or Costa Rica), these new Internet sportsbooks conduct business with less regulation, lower tax rates, fewer licensing requirements, and little to no threat of legal prosecution vis-à-vis online sportsbooks in jurisdictions with stricter laws and policies.

Copyrighted material

B Market Shares

The Internet sportsbook industry is currently in a state of flux for a number of reasons. As the market for online sportsbooks matured, the number of virtual sports gambling portals increased rapidly and subsequently stabilized. Whether this trend will continue is unclear because of the increasing threat of prosecution and the uncertainty with which it is associated. For example, on May 23, 2011, an American federal grand jury returned indictments charging various online sports betting businesses and individuals with illegal gambling and money laundering (Millman 2011). The domain names for 10 online sportsbooks were seized, including the popular website Bookmaker.com. Several prominent online sports betting portals responded to the crackdown by rerouting traffic to domain names with different website suffixes, such as .ag or .eu instead of the ubiquitous .com.

Wilson (2003) cites 1,122 gambling websites in June 2001, though his number likely includes non-sports-related gaming sites as well. In the summer of 2007, SportsbookReview.com (SBR) graded 755 sportsbooks as acceptable and 886 sportsbooks as blacklisted, which in this context refers to a sportsbook that has liquidity problems and/or may be fraudulent. In June 2011, according to SBR, the number of blacklisted sites increased to 1,052 (many presumably have since closed down) and 579 other sites were currently in operation. Accurate revenue figures are impossible to establish in this industry due to existing regulations (or lack thereof) and an absence of incentive to disclose financial figures. Estimates by Christiansen Capital Advisors (CCA) indicate enormous growth in the industry.¹³ Revenues increased from USD3 billion in 2001 to an estimated USD18 billion in 2007. These figures include non-sports-related gambling but nonetheless provide some insight into the growth of the industry. Time will tell how new legislation affects the industry's expansion. In the post-Internet era, sportsbooks operate in complete autonomy compared to U.S. corporations. If nothing else, local land-based bookmakers now face increased competition, though there is some evidence that terrestrial gambling companies support online betting (Richtel 2001).

C Product Differentiation

In the pre-Internet sportsbook market, a bookie would only collect money after the sporting event was over. Thus the burden of establishing credibility lay solely on the bookie, who had to decide if a gambler was worthy of credit. Information gathered by the gamblers about the bookies was obtained by word of mouth and only really concerned the bookies' reputations of paying out any winning wagers. In contrast, Internet sportsbooks require fully funded accounts to be set up by gamblers before they place wagers. The burden of establishing credibility has shifted to the gambler, who must establish that the sportsbook site will pay out on wins. In addition to financial credibility, gamblers must be concerned also with the stability of the

Copyrighted material

Internet sportsbook as legislative bodies attempt to regulate the industry. Information gathered by the gamblers can take many forms, including rating websites, such as SBR, that the credit worthiness and customer service track record of each Internet sportsbook.

Classic signs of competition in the marketplace have appeared online, for example, the introduction of new forums for gambling. The traditional system of a bookmaker setting odds that a gambler wagers on has been challenged by online exchanges that act more like stock exchanges than traditional sportsbooks. Instead of the traditional gambling methods, online gambling can now take the form of playing the bookie or investing in a predictive market. Also, one would expect the product's price to decrease as competition is introduced. This reduction in the price of gambling has taken place as online sportsbooks have begun to decrease the vigorish they take in. Aside from the new predictive market forums, traditional sportsbooks also offer more types of wagers. In-game style sports betting (wagering on a game while the event is taking place) has increased in popularity. Research has found that such real-time markets operate just as efficiently as traditional wagers (Debnath et al. 2003).

D Demand Elasticity

Due to the elimination of geographical restrictions, demand is more elastic to price in the post-Internet sports gambling era. Currently, small point-spread fluctuations change bettor tendencies, as bettors can have multiple accounts and move quickly from sportsbook to sportsbook. In addition, if the point spread differential is too great, there exists the opportunity for what is known as arbitrage, in which a bettor wagers on both sides of a game with different point spreads (Griffin 2011). If the game in question results in a score between the two spreads, the bettor wins both wagers. This kind of activity creates an incentive for sportsbooks' point spreads to converge. The end result is multiple firms with prices (or point spreads) very close to each other and the end of third-degree price discrimination, as we would expect in a more competitive economic environment.

E Economies of Scope

Some economies of scope do exist between the Internet sportsbook industry and other Internet gaming industries. An Internet sportsbook will often offer more traditional Internet games, such as blackjack, slots, or poker. Calls to regulate the industry could not be more understandable in this case, as the recreational gambler likely has no idea of the true expected payouts, which in regulated terrestrial gambling casinos are closely monitored (and transparently displayed). Overall the impact of the economies of scope compared to the terrestrial games has greatly decreased.

F Sportsbook Efficiency

In the classic framework of the sportsbook, the objective was simple. By balancing the action on each side of the game the sportsbook is guaranteed no risk and a safe (5% on all action) return. Recent literature has challenged this assumption, a change likely attributable to greater competition in the online sportsbook industry. Steve Levitt (2004) has suggested that oddsmakers adjust the lines to take advantage of their superior forecasting ability, a suggestion supported by Wayne Winston (2009). George Diemer (2009) followed up this research and identified two types of sportsbooks, a profit-maximizing type and an exposure-minimizing type. Rodney Paul and Andrew Weinbach (2011) also found imbalance but attributed it to bettor's bias toward the favorite teams. Deniz Igan, Marcelo Pinheiro, and John Smith (2011) highlighted bookies' recognition of bettor racial biases as influencing unbalanced books and the initial setting of point spreads. No matter the cause, the assumption of the traditional terrestrial sportsbook's balanced action is being reevaluated.

G Online Sports Betting Exchanges as an Anti-Corruption Tool

Stephen Easton and Katherine Uylangco (2010) found a high level of efficiency in the online tennis betting market, making it a useful predictor of match outcomes. Given the betting market's forecasting ability, it could be used as a statistical screening device for nefarious conduct in the market. Similarly, Karen Croxson and J. James Reade (2011) pinpointed prompt and accurate price updates in the online soccer wagering market following any change in scoring, indicating considerable market efficiency. Unexpected deviations from the documented efficiency could trigger a follow-up investigation regarding whether such deviation was benign or indicative of chicanery. Using Betfair-derived data, Alasdair Brown (2012) found trace amounts of inside information in trading during the epic 2008 Wimbledon men's final between Roger Federer and Rafael Nadal. Betting exchanges such as Betfair have also contributed to the detection of corruption in sport (Drape 2008). As quoted by Davies et al. (2005, 539), a Betfair spokesperson said, "We are putting a searchlight on the sport and helping it clean up its act. There is a clear paper trail on our site that doesn't exist in high street [betting] shops. We are entirely transparent. We have no vested interest in the outcome of a horse race" or other sporting event.

In 2007, Betfair detected suspicious betting patterns involving a tennis match between Russian Nikolay Davydenko and Italian Martin Vassallo Argüello and took the then unprecedented step of halting further trading on the match and turning over transaction records to the appropriate tennis authorities. The subsequent investigation cleared both players of wrongdoing but resulted in Ben Gunn and Jeff Rees's (2008) "Environmental Review of Integrity in Professional Tennis," which (1) identified 45 matches

Copyrighted material

with *prima facie* evidence of fraud that merited further inquiry and (2) led to the establishment in 2009 of the Tennis Integrity Unit (TIU), a joint venture of the International Tennis Federation, the four Grand Slam tournaments, the ATP World Tour, and the Women's Tennis Association, each of the governing bodies in global elite-level tennis.¹⁴ The TIU rendered its first significant enforcement action on May 31, 2011, when the organization placed a lifetime ban on Austrian player Daniel Kollerher for gambling-related match-fixing.

IV THE FUTURE OF THE INTERNET SPORTSBOOK INDUSTRY

Sports gambling is now in its third incarnation. The first generation of sports gambling has existed for centuries. Whether the wagers take place directly between bettors without an intermediary, at a government-regulated brick-and-mortar establishment, or through a neighborhood bookie operating illegally, this first-generation sports betting continues to be popular. The second generation of sports-based gambling was described by Steven Crist (1998) in a *Sports Illustrated* cover story that reported on bettors placing wagers based on fixed odds remotely through the Internet. By offering odds, point spreads, totals, and other wagering opportunities, online (and often offshore) sportsbooks mimicked terrestrial sites in Las Vegas and were more convenient because they do not require the bettor to be on-site to place a wager.¹⁵ During this time, only one American sportsbook operator conducting business offshore was convicted by a jury of violating the Wire Act,¹⁶ and only one individual bettor was charged with placing a sports wager over the Internet.¹⁷ The third generation, sports gambling 3.0, characterized by real-time online betting exchanges with attributes analogous to any modern stock exchange, has been described by Smith and Vaughan Williams (2008, 404–405) as “an interactive web-based platform for placing and laying bets on sporting events” that offers in-running markets and lower commission rates. Betfair in London is the most recognizable (and popular) example of a sports betting exchange (Davies et al. 2005). Recognizing this as a potential growth area, at least one land-based, in-person sportsbook, Cantor Gaming’s upscale M Resort in Las Vegas, has begun offering similar options for patrons (Benston 2010). Given this backdrop, a number of noteworthy developments over the course of the past decade have illustrated the uncertainty currently associated with Internet gambling and the online sportsbook industry.

A BetOnSports.com

No case study explains the uncertainty in the industry as well as what transpired in connection with BetOnSports.com. Between 2002 and 2004, the Costa Rica-based

company listed on the London Stock Exchange took in almost USD4 billion in wagers, 98 percent of which came from Americans. On July 17, 2006, company CEO David Carruthers was arrested at the airport in Dallas, Texas, en route to Costa Rica. He was charged with racketeering, conspiracy, and fraud connected to an illegal gambling enterprise. In addition, the government charged BetOnSports.com founder Stephen Kaplan with multiple counts of promoting illegal gambling. These charges illustrate how current laws are being enforced in connection with Internet sports gambling businesses and are suggestive of how future cases may be prosecuted.

B Unlawful Internet Gambling Enforcement Act of 2006

The latest attempt by Congress to curtail sports gambling was made in October 2006, when it passed the Unlawful Internet Gambling Enforcement Act (UIGEA) as part of an otherwise unrelated anti-terrorism bill.¹⁸ UIGEA was signed into law in 2006 but did not go into effect until June 1, 2010. The statute's preamble acknowledges: "New mechanisms for enforcing gambling laws on the Internet are necessary because traditional law enforcement mechanisms are often inadequate for enforcing gambling prohibitions or regulations on the Internet, especially where such gambling crosses State or national borders."

UIGEA prohibits payment processing entities, such as banks and credit card companies, from accepting or distributing monies derived from gambling (Ramasastry 2006). Prior to UIGEA, a gambler could fund his or her account by using a credit card. The intent of Congress was to eliminate the ease of financing overseas sports gambling and to cut sportsbooks' liquidity. A number of Internet gambling sites responded by withdrawing from U.S. markets. Certain private websites continue to access the American market, but they face the threat of prosecution. Similarly, bettors with money on deposit risk being unable to redeem their winnings and account funds if the website is shut down and assets are seized.

UIGEA contains a number of important exemptions. Such carve-outs include wildly popular online fantasy sports, government-run lotteries (some of which have intellectual property licensing deals with professional sports teams and leagues), entirely intrastate gambling, certain interstate horse racing, and gambling taking place on Indian reservations. The indirect anti-gambling enforcement mechanism inherent in UIGEA and the numerous exceptions to what is defined as "gambling" therein have resulted in a situation described as "the absence of a comprehensive federal policy toward internet and sports wagering" (Cabot 2010, 271), "the troubled legal status of internet gambling casinos in the United States in the wake of [UIGEA]" (Nelson 2007, 39), and "an exercise in futility" (Kelly 2011, 257). In addition, Jennifer Chiang (2007) highlighted how compliance with federal laws such as UIGEA may still result in violations of state law. Finally, the passage of UIGEA has re-ignited calls for Internet gambling to be regulated at the state, not federal, level (Wajda 2007).

Copyrighted material

C Galileo Fund

The proliferation of online sportsbooks and the accompanying decreased concentration of market power have resulted in a considerable increase in the number of “outs” available to both casual bettors and professionals who make a living wagering on sporting events. Such professional bettors gamble systematically in a way resembling stock market investors and include individuals with large bankrolls as well as syndicates using sophisticated computer-driven algorithms. Accordingly, it was only mildly surprising when Gibraltar-based Quay Financials and London-headquartered Centaur introduced the Galileo Managed Sports Fund (Galileo), a hedge fund intending to focus on the sports exchange market (Millman 2010; Popper 2010; Wachter 2010). Darren Rovell (2010) reported that Galileo would bet on outcomes in “soccer, tennis, cricket, horse racing and golf, with plans to expand to [American football] and baseball over the next year.” The minimum initial investment in Galileo is €100,000. As of June 1, 2011, Galileo did not accept investors from the United States, although fund managers were reportedly seeking the government’s stamp of approval.¹⁹ If the Galileo fund is successful (in terms of investment volume and returns), online sportsbooks and exchanges almost certainly will respond.

V CONCLUSION

The Internet sportsbook industry is in transition. As some American-based sports leagues shift to tepidly supporting legalized gambling (McKelvey 2004a, 2004b; Thomson 2009), the sometimes polarizing discussion continues regarding the (beneficial and detrimental) impact gambling has on economies and financial systems (Kindt 2010). Future legal developments, in both the United States and elsewhere, will continue to shape the industry (Cabot 2010; Chan 2010). Absent American intervention in the form of legislation and prosecution, the Internet sportsbook industry will probably converge toward a competitive industry with normal economic profits and wagering options available to the consumer. That likelihood notwithstanding, government regulation for U.S.-based bettors and sportsbooks would almost certainly be welcomed by those in the Web-based sports gambling industry, as such oversight would likely increase the legitimacy, transparency, and long-run certainty for the industry globally.

NOTES

1. Three other U.S. states (Delaware, Oregon, and Montana) are permitted to offer limited-scope sports wagering under the Professional and Amateur Sports Protection Act of 1992 (PASPA) (Galasso 2010). Although largely outside the scope of this book chapter, it is noteworthy that a lawsuit brought by a New Jersey senator and an Internet gaming trade

Copyrighted material