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International trade in gambling services: between prohibition and regulation

In recent years gambling has become very important economic activity. In 2015, the size only of the global online gambling market had a volume of 35.5 billion U.S. dollars¹. The global gambling market, online and offline, is expected to grow at a Compounded Average Growth Rate (CAGR) of 7.91% in the period 2016 – 2020².

The current situation subsists in the restrictive national regulations that cause the growth of the “grey market” of gambling services (e.g. displacement of online gambling websites in the most favourable jurisdictions). It seems necessary therefore to recognize the existence of international trade in gambling services without the historical and moralistic prejudices that dominated the gambling industry for centuries. Abandoning prejudices it becomes possible to think of building an international regulatory model giving more certainty for operators and the best protection against fraud, money laundering and criminality.

Such regulation should be flexible to allow countries to maintain discretion over the forms of gambling they permit at the national level. This is necessary because the most popular justification of the countries to refuse international regulation of gambling services is cultural differences. This regulation should also be capable to offer an effective enforcement against violations.

It should answer or give address to the questions related to taxation and jurisdictional issues.

Current situation

Living the era of globalization, when individuals may migrate, and to behave in accordance with the law of the country of new residence, new technologies, however, help to provide services without leaving the jurisdiction of origin. In these circumstances, is it still possible to say that services (and gambling *in primis*) can be regulated at the national level? The nature of Internet and the current situation when the regulation is limited to the national borders makes it obvious that the effort should be made at International level.

Current situation is characterized by some concerns and justifications offered by different countries as a basic motivation against the International regulation.

The most popular concern is about *moral, cultural differences and opposite views on gambling*. Different gambling cultures existed in the past, but these differences have been overcome in other

¹ European Gaming and Betting Association / <http://www.egba.eu/facts-and-figures/market-reality/>

² Global Gambling Market 2016-2020 / http://www.researchandmarkets.com/research/v7fxbk/global_gambling

fields. Why it's not possible to do in gambling? Are these differences still so important in globalized XXI century society?

There is a range of activities that countries find morally objectionable and attempt to block. Morality-based restrictions can also extend to Internet filtering all content considered inconsistent with social norms, such as gay rights, religious views and gambling. References to morality and social norms can be used to justify restrictions on a wide range of activities.

The other popular justification is *protection against addiction*. Countries that invoke these considerations often have their own state-run gambling monopolies that organize advertising and expansion of gambling. The protection against addiction seems to be better regulated at the International level due to the transnational nature of Internet and the use of new technologies. Today's gambling transactions even in the betting shops overcome national borders.

Protection of minors is also of great concern. However, without regulation minors are more likely able to gamble.

The third popular justification is *protection against fraud*. It seems that the fraud mechanisms are not so different in the USA and in Malta. The needs in terms of information and transparency are not differ from one country to another. Valid thesis may be concern about not the same consumer protection level offered by online gambling as offered by land-based establishments. Still the thesis is valid in absence of the prohibition or regulation (and effective control) that is imposed on "physical" establishments.

The fourth justification is *protection against crime*: it is really difficult to explain why regulation should be kept at the national level. Protection against all kinds of criminality surely is not possible if regulated at the national level. Criminality is an international issue and many International agreements in different fields confirm it.

All these issues are serious, but it's also true that protection against addiction, fraud and crime is easier because of the use of Internet. The technology creates a record every time for every gambling transaction and it could be complied to identify patterns of addictive or criminal behaviour for both gambler and operator. Some organizations in the field of gambling have already proposed ideas such as creating international databases that could screen and identify addictive players, minors, etc.

Another serious problem is not publicly declared, but still of concern of the countries is related to the tax revenues reduction. Gambling generates significant revenues and therefore liberalized gambling would provoke a decline in tax revenues. However, it already happens with illegal or online gambling websites from other countries that provoke serious tax revenues reduction for the countries.

The other serious problem is restrictions on information flows which affect online gambling services. Such restrictions are commercial in nature and they reduce the ability of buyers and sellers to transact and companies to operate across borders. In many cases, these restrictions are

driven by the success of foreign Internet-based activities as governments seek to replicate their successes by protecting domestic activities from foreign competition. These commercial Internet restrictions include routing traffic to domestically owned companies, blocking particular sites or degrading Internet access enough that users turn to alternative and usually domestic websites³. For instance, the foreign company may not be aware that access to its website has been blocked⁴.

Different approaches make any regulatory or prohibitive model impossible unless all states are to regulate or to prohibit. The use of Internet not only for online gambling, but also for land-based gambling (e.g. betting shops) dissolves regulation limited to the national borders.

Seems important to notice that organisation of games of chance is prohibited by legal systems of all EU Member States. At the same time, most legal systems in Europe permit certain derogations to this *a priori* prohibition, the central historical reason being that complete prohibition has proven ineffective and has led to illegal and completely uncontrolled organisation of games of chance. EU Member States have thus realised that it is for reasons of having control over the games better if certain games may be organised, however, under strict state control. The latter is held at three levels – by controlling gambling operators, by providing legitimate types of gambling and by protecting the players – consumers⁵.

In light of the above, it seems unlikely that countries will prefer to establish the prohibition.

First of all, because the countries that already successfully regulate gambling will adamantly oppose the International prohibition. These countries already receive significant tax revenues from regulated gambling.

The next reason is that prohibition will create an enormous “black market”. The ban of gambling services could discourage the operators based in prohibiting countries, but these prohibitions would have no effect on foreign online gambling operators. Gamblers could easily avoid identifying their location in several modes before logging into a foreign gambling platform. It has been noticed that prohibition of online gambling may have negative effect. Respected operators are unwilling to jeopardize their land-based operating licenses by allowing irregularities on their websites. In case of prohibition, respected operators will leave and in their absence, unlicensed, unregulated gambling operators would try to take the opportunity for greater profits in the face of diminished competition⁶. Therefore the prohibition is more likely to exacerbate problems like frauds, crime and underage gambling. There are opinions that consider prohibition to make the situation worse. The regulatory authorities, in practice, would have little effect other

³ Meltzer, J.P. The Internet, Cross-Border Data Flows and International Trade (<http://onlinelibrary.wiley.com/doi/10.1002/app5.60/full>)

⁴ See United States's request to China for information under paragraph 4 of Article III of the WTO General Agreement on Trade in Services.

⁵ Luik, D., Hojnik, J. Gambling Regulation in Slovenia: from Adapting to Socialist Morality up to EU Free Trade Environment // <http://ssrn.com/abstract=2834282>

⁶ Loscalzo, T. Internet Gambling Policy: Prohibition versus Regulation, 7 Jeffrey S. Moorad Sports L.J. 11 (2000).

than to scare away scrupulous operators, leaving behind only those that are willing to break the law to satisfy a very real consumer demand⁷.

The prohibition is also contrary to the concept of capitalistic exchange and to the liberal culture: freedom of gambling was seen as a fundamental prerogative of the individual since the Modern period.

Therefore, considering the analysis above and the use of Internet in today's gambling services, seems clear the need to establish the regulatory model. Its effectiveness will depend on an international agreement which among other establishing a sufficient international cooperation involving multiple countries. That's why there is hope that UNCITRAL could intervene with this initiative.

Model proposal

The model requires the presence of two basic elements: regulation and international cooperation.

History shows that the problems related to the development of communications have already pushed toward internationalization: examples of International Telegraph Union (1865), which continues to exist as the International Telecommunication Union; Universal Postal Union (1874) and others. Even then the unions were created to resolve the tensions between the free flow of information and the sovereign rights of States to control the cross-border flow. As we can see, information-related problems are the same as those of 100 years ago.

The discussion on whether liberalisation of gambling would be detrimental to citizens can be eternal; it is nevertheless true that uniform approach to all types of gambling is not the right approach. Gambling is a very complex sector of services, as regards various methods of playing as well as their social consequences. In times of cross border television and internet, when citizens of one country follow all major national football (and other sports') leagues in the world, it is probably unsound to limit their access to sport bets to national sport events only⁸.

The international regulations should be very flexible to be accepted by a wide range of countries. It should be territory based which will give possibility to the countries to license gambling operators. As it clear, the countries will agree the international regulation only if this regulation would preserve individual economic and cultural policies as well as moral standards of each member of such regulation. A very lax basic international regulation would allow anyone to provide online gambling services within the country and affect the revenue that country would receive from its own gambling market. Also, if the standard was too strict and deterred providing services across borders, it would be no different from the current situation.

⁷ Karadbil, J.F. Casinos of the Next Millennium: A Look into the Proposed Ban on Internet Gambling, 17 ARIZ. J. INT'L & COMP. L. 413, 419 (2000).

⁸ Luik, D., Hojnik, J. Gambling Regulation in Slovenia: from Adapting to Socialist Morality up to EU Free Trade Environment // <http://ssrn.com/abstract=2834282>

Seems evident that there would need a cooperation between countries in determining the range of regulatory policies not so diverse so as to provoke the movement to tax and legal “heavens” as well as comparable legal and tax structures so that operators prefer not to move.

Conflicts between countries are possible not just between liberal and conservative countries in terms of gambling regulation, but also between small and large countries. Countries with large internal markets and thus a prevalence of domestic gaming customers typically try to limit the offering of games by imposing high taxes. Smaller countries and economies with proportionally small internal markets, which rely largely on customers from other economies, are prone to offer low tax burdens and thus encourage gaming operators to create a more comprehensive non-gaming tourist amenities in order to export gambling and non-gambling services as much as possible and maximise the economic benefits with minimal negative social impacts⁹.

The regulation could be based on possible solution in the regulation of gambling services elaborated for the European Union.

First part should be the introduction of the analogue of the EU “minimum harmonization”. The minimum harmonization occurs when the European Union adopts a minimum standard to which all Member States must subscribe, while also allowing individual Member States to impose higher standards on goods that will be either produced within the country or imported into the country. Minimum harmonization provides the baseline, but is also flexible by allowing for higher standards within each Member State based upon the national interests that any individual Member State may have.

Adopting “minimal harmonization” of gambling services at the International level the countries once signed the agreement, could not ban gambling services (first of all, those online) from other participating countries, provided those services complied with the criteria established by such agreement.

The other part could be the mutual recognition. Mutual recognition is the principle that when a product or service is legally manufactured in one EU Member State, it may be freely offered in other Member States, irrespective of whether it complies with the national legislation in that country. Specifically, national legislation cannot prohibit the introduction of a similar foreign good made with standard equivalent to that enforced in the host Member State. Thus, applying this model to International level, if a country provides an equivalent gambling service, then theoretically it should be allowed in the host country where it is being offered. For example, a private business operating in Italy would be able to provide its services within USA. USA would have to allow the gambling services from Italy, but it could also expand its operations into Italy. This would create a competitive regime where only the best gambling services would survive, which presumably would be those that are the safest and securest for their customers.

The best solution for International regulation would be two-fold. UNCITRAL could institute a standard similar to the “minimum International harmonization” coupled with a mutual recognition

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strategy. If the minimum standard is relatively high, protective countries would be more likely to sign on and ensure the standard's passage. Also, through the mutual recognition strategy, countries would have to allow gambling services once the services met the minimum standard or, if in place, the higher one set by the host country.

Another interesting example of gambling regulation that can be basis for international regulation of gambling services is Australia. Since the 1980s, Australia has deregulated and largely deindustrialised its economy. As state and territory governments found themselves subject to shrinking taxation revenue, commercial gambling has paradoxically offered certainty and an independent source of income to cash-strapped jurisdictions reliant in large part on federal largess¹⁰. As such, by 2008–09, gambling accounted for 10% of total own-state tax revenue¹¹.

International model should have some specific characteristics and be very accurate in some points.

It should be flexible enough to satisfy the parameters which differ from one country to another. Probably, if the model would establish licensing process, the individual countries should be able to decide the number of licenses they would grant. However, this solution seems unacceptable, because some countries could decide to grant a really restricted number of licenses and this would not be so different from the current situation. Still the lack of autonomy will be crucial, because countries would be unwilling to submit to such International model.

The model should also foresee the basic rules of taxation, possibly avoiding situation when gambling operators will be moving to “tax heavens” offered by some countries participating in the agreement.

It should establish a basic standard of regulation that would prohibit underage gambling, mandate self-exclusion mechanism and protect privacy. For this reason the regulation model should require the registration of gambling activities (both land-based and online) with local authorities or an International governing agency established by the agreement. It could guarantee the transparency and disclosure of information like slot machine payouts, server calculations of bets and other type of information.

International model of gambling services regulation created taking into account points indicated above, could be effective not only in protection of consumers, but also in preventing money laundering and crime.

UNCITRAL proposing an international agreement on regulation of gambling services, could be the link in the negotiations through which countries can line up their gambling policies to the level that any remaining differences don't make the international regulation model ineffective.

¹⁰ Markham, F., Young, M. “Big Gambling”: The rise of the global industry-state gambling complex. // <http://dx.doi.org/10.3109/16066359.2014.929118>

¹¹ Productivity Commission. (2010). Gambling, Report no. 50. Canberra: Productivity Commission, p.2.11

The UNCITRAL initiative to create model provisions on gambling services, an effort which could draw upon experiences from around the world, can be able to mark a turning point for the international regulation of gambling services. Through this initiative of UNCITRAL, policymakers of many countries will be able to look abroad, not to be bound by foreign law, but rather more practically to learn from successes and failures in foreign attempts to regulate gambling services.