

TESTIMONY OF

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ON

CAN INTERNET GAMBLING BE EFFECTIVELY REGULATED TO PROTECT  
CONSUMERS AND THE PAYMENTS SYSTEM?

BEFORE

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON FINANCIAL SERVICES

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2128 RAYBURN HOUSE OFFICE BUILDING

Mr. Chairman and Distinguished Members of the Committee

## **Introduction**

I am Craig Pouncey, a partner in the Brussels office of UK law firm Herbert Smith, and head of my Firm's international trade law practice. In that capacity, I have had the opportunity to work on the case between Antigua and the United States, in which the WTO found that a number of U.S. laws violate the General Agreement on Trade in Services ("GATS") because they prohibit the supply of Internet gaming services from jurisdictions outside the U.S.

I do not currently represent Antigua but act for a number of EU companies with an interest in the gaming sector.

In this testimony, I will explain the role of the WTO in the Internet gambling debate and the different options that the U.S. has in the WTO, following its loss in the Antigua case.

## **General background and the Antigua dispute**

The GATS, which is the relevant WTO Treaty here, works on an "opt in" basis. This means that key obligations only apply to the extent that a country has "opted in" for a specific sector (or, in GATS language, made "specific commitments"). In the case brought by Antigua, the Appellate Body of the WTO found that the U.S. had made "specific commitments" with regard to the cross-border supply of gambling and betting services. As a result, the U.S. had to provide "market access" to the suppliers of such services from other WTO member countries. The Appellate Body went on to find that the U.S. violates that obligation because several federal laws prohibit the use of the Internet to supply gaming services from foreign jurisdictions to consumers in the U.S.

By way of defence, the U.S. had invoked an exemption clause that allows a country to depart from its normal WTO obligations (*i.e.* in this case to prohibit access to Internet gaming services from countries such as Antigua) because of the need to protect public morals. The U.S. argued that Internet gambling posed uncontrollable risks of youth gambling,

fraud and money laundering. This defence failed, however, because the U.S. allows Internet betting on horse races.

The U.S. was given until April 3, 2006 to comply with the findings of the Appellate Body Report. On July 6, 2006 Antigua convened a WTO "compliance Panel" to assess the steps taken by the U.S. to comply with the Appellate Body's findings. The U.S. used these proceedings, *inter alia*, to reargue its case that Internet gambling cannot be regulated and that Internet horse race betting was not lawful in the U.S. The U.S. lost the argument again and, on March 30, 2007, the latest WTO report in this saga was issued. In the context of this debate, the most interesting points of this most recent WTO Report are the following:

- The WTO Panel found that "there are at least 18 State laws that expressly authorize wagering by wire within the United States, including on a wholly intrastate basis".
- The WTO Panel states that, while the U.S. originally argued that Internet gambling could not be regulated, it has changed its position because the Unlawful Internet Gambling Enforcement Act 2006 explicitly acknowledges that such regulation is possible.
- The WTO Panel refers to the recent prosecution of foreign Internet gaming operators but adds that it finds it "striking" that the DOJ has never prosecuted any of the U.S. based operators of Internet horse race betting.
- The WTO Panel notes that the U.S. had an opportunity to clarify that Internet gambling on horse race betting is prohibited but that the Unlawful Internet Gaming Enforcement Act does precisely the opposite by deliberately maintaining the ambiguity.

The U.S. recently decided not to appeal this latest WTO report, which, therefore, became final.

### **Option 1 for the U.S.: withdrawal of commitments**

On May 4, 2007, the USTR announced that the U.S. would start a procedure to withdraw the U.S. commitment on gambling and betting services. Pursuant to this procedure, all WTO Members, not just Antigua, are entitled to claim compensation from

the U.S. Such compensation normally adopts the form of additional trade liberalisation in other areas. This procedure has never been used in a context such as the one at issue here and the U.S. move is generally perceived as an attempt unilaterally to change the WTO contract after losing the legal fight.

The USTR press release announcing the withdrawal of the GATS commitment mentioned that, in its view, other WTO Members have "very little, if any" basis to claim compensation because the U.S. made the commitment on gambling by mistake.

It is unlikely that other WTO Members will share the U.S. view on this matter. First of all, they may well find it difficult to believe that the U.S., which was the main driver of the GATS negotiations during the original negotiations, was unable to understand its own commitments.

Further, it should be noted that the U.S. has requested, obtained, and used the right to impose countermeasures in a WTO dispute settlement case where such a "misunderstanding" had effectively occurred. In the well known *Bananas* dispute between the U.S. and the EU, the U.S. argued that the activities of U.S. companies such as Chiquita were "banana distribution services" covered by the GATS and the EU's GATS commitment on "distribution services".

The EU disagreed. In fact, the EU had taken a series of measures to protect its banana regime from being challenged in the WTO but it had never considered that its commitment on "distribution services" could have been used against its regime for the importation of bananas. If the EU had realised this, it would no doubt have excluded "banana distribution services" from its commitment on "distribution services". However, the EU had not done that and thus lost the dispute with the U.S. The U.S. then obtained the right to impose painful economic sanctions on the EU for a total value of USD 191.4 million per year. This caused very serious hardship to the EU companies targeted by those sanctions and, in at least one case that I am aware of, it caused bankruptcy. The total amount of these sanctions related to a lack of compliance with GATS obligations which the EU never intended to make.

The same U.S. that requested, obtained, and applied these economic sanctions *vis-à-vis* the EU is now claiming that it can withdraw commitments without compensation because *it* did not intend to make these commitments. In my view this is wrong as a matter

of law. I am convinced, therefore, that a number of WTO member countries will take the same view and seek compensation from the U.S. I also believe that the U.S. will be asked, as a result, to open up other markets. This will be the price that the U.S. has to pay to avoid option 2, *i.e.* regulation of Internet gambling.

**Option 2 for the U.S.: regulation of Internet gambling**

Appropriate regulation of Internet gambling would put the U.S. on a road to resolving the WTO problem. The U.S. would avoid having to offer possibly substantial compensation in the form of opening new markets to foreign competition, and, as a result, affecting possibly numerous other economic players in the US who have absolutely nothing to do with gambling, or the WTO gambling dispute. Further, rather than losing credibility, the U.S. would strengthen the WTO and its legal system, which the U.S. wants other countries, and in particular China, to respect.

Thank you, Mr. Chairman and Distinguished Member of this Committee for considering this testimony and I would be happy to answer any questions that you may have.