



House Financial Services Committee Hearing

“Can Internet Gambling be Effectively Regulated to Protect Consumers and the Payments Systems”

June 8, 2007

Statement for the Hearing Record

Submitted by Mary Williams, Chief Secretary, Isle of Man Government

Chairman Frank, Members of the Committee, the Isle of Man Government welcomes the opportunity to submit written testimony to your Committee.

Summary

The on-line gambling industry is now a legitimate business recognised by banks, stock markets and investors and one that is increasingly based in well-regulated jurisdictions.

The Isle of Man has been at the forefront of introducing legislation regulating the on-line gaming business. The Isle of Man is in a position to attract the best businesses in the world because it has adapted to the new on-line gambling environment.

It is of paramount importance to the Isle of Man that the industry is well regulated to protect persons under the age of 18 and the vulnerable, to ensure gambling is fair, and to prevent the use of the gambling sites by the criminal fraternity and terrorists.

The Isle of Man believes the best way to achieve this is to ensure such businesses are well regulated and not pushed further off-shore by prohibitionist actions which will be to the detriment of Governments, customers, and the vulnerable as well as to the benefit of terrorists and organised crime.

All Isle of Man gaming companies have surmounted strict compliance procedures including police, Treasury and data protection checks on individuals as well as their companies. In addition, the Island's Gambling Control Commission will have approved both the games and the underpinning software. Tough money laundering rules - including "know your customer" practices - will be enforced, to parallel the Isle of Man's strict and internationally recognised financial services regulation.

The Isle of Man wishes to work with the other jurisdictions including the United States so that its licence holders are not in contravention of the laws of the United States and other jurisdictions and therefore, to provide fair workable solutions to obtain access to worldwide markets.

On-Line Gambling Regulation Act 2001

Gambling is defined under Isle of Man legislation as all types of gambling including casino games, sports bets, lotteries etc. "Betting" is distinguished as being limited to sports betting, and "gaming" includes casino type games and lotteries.

In June 2000 it was decided to permit the extension of on-line betting to include other on-line games such as those available in land-based casinos. As a result of this decision, endorsed by the Isle of Man's Council of Ministers, the On-line Gambling Regulation Act became law in May 2001.

The decision to extend the limit of on-line gambling transactions was based on the need to extend the Island's economic base into a new area of business that was growing at a rapid rate. The advantage the Isle of Man could exploit, at the time, was that the larger gaming companies wanted to be involved in the on-line business, but only in a well regulated jurisdiction and thereby compete with small specialised companies that had set up in jurisdictions with limited regulation.

The reputational risk to the Isle of Man was a paramount concern, and it was decided that only if the reputational risk could be kept to an absolute minimum would the Isle of Man involve itself in this new area of business. One of the main requirements at the time to reduce reputational risk was the provision of a licence condition that prevented any on-line gaming company taking bets from jurisdictions where such on-line gambling was deemed illegal.

Also at this time, a number of the on-line businesses that were locating to the Isle of Man had U.S. regulators for their land-based operations and, therefore, the Isle of Man took a cautious view on the legality of taking such bets. Although it was left to the individual operators to ensure they were acting within the law of jurisdictions from which they were taking bets, it was known that the Isle of Man Government's stance, at the time, was that bets should not be taken from the United States.

The On-line Gambling Regulation Act is designed to do the following:-

- Make all on-line gambling conducted from the Isle of Man without a licence illegal whilst permitting licensed interactive gaming on the internet on a tightly regulated basis which is considered key to the success both for companies providing services and for the Island itself.
- Provide a secure regulatory regime, involving the following Agencies in the Isle of Man: the Gambling Control Commission ("the Commission"), the Financial Supervision Commission ("the FSC"), Data Protection, Customs and Excise and the Isle of Man Constabulary.
- Limit licence holders to offering only games that are approved by regulation. Not all games are available to all licence holders. This ensures each licence holder is competent to provide each game licensed to it.

- Ensure companies are registered in the Island, their designated official or operations manager are resident here, and that licence holders maintain sufficient financial reserves or a bond in the Isle of Man to pay customers in the event of financial problems. Regulations protect players' privacy, prohibit sales to minors, prevent money laundering and the use of on-line sites in relation to any movement of monies for terrorism purposes. There are also other player protections within the Act, such as gaming contracts being enforceable in law, codes on advertising and accuracy of web-site claims and regulations governing the conduct, fairness, and probity of gambling on the site. The regulator also has rights of entry and powers to inspect software and all gaming transactions.

The Act is considered to provide an important opportunity for the Island to benefit from a growing e-commerce market, but the Island's reputation for probity has to be protected. That is why regulation is given such emphasis within the Act.

The number of licences was initially restricted to three to avoid overburdening the new regulatory system whilst it became established. This restriction was raised to thirteen and is currently being removed.

Consequences of the On-Line Gambling Regulation Act 2001

As a result of the new legislation, the Isle of Man was successful in attracting household names from the international gaming industry, including companies such as MGM, Rank and Kerzner. However, despite the well-known brands, the Isle of Man licence holders were unable to attract enough business to their sites. Additionally, the cost of complying with the regulations under which the licensees operated made it uneconomic to carry on gaming businesses.

The result was that the high-profile names either closed down their operations or re-located to jurisdictions where regulation was less burdensome or from where they could take bets from the United States.

Since the departure of the major licence holders, the Isle of Man has been re-examining its regulation and in particular the manner in which it requires software to be tested. In this connection the software is considered to meet the regulatory requirements if it has been certified as such by a major accountancy firm or a specifically approved testing house. In addition, testing is carried out on a result-based basis to ensure the systems meet regulatory requirements.

A new system has now been put in place that will accomplish the Government's aims whilst providing a commercially viable approach to software testing which is:

- a) where certain companies are certified to undertake testing by the Department of Home Affairs ("the Department") (such as the large accountancy firms and the premiere software testing companies (known as certified testing companies)), they are able to test the software of licence holders and certify that the software is fully compliant with the regulations;
- b) once the certificate has been received and licence conditions have been complied with, such as putting in place a bond, the licence comes into force;

- c) the Commission is then responsible through the accountancy firm, statistician and other technical experts employed for regulating and monitoring the site by requesting periodic reports which are examined by the experts for regulatory compliance. This is known as result-based testing which identifies any problems by measuring output figures against house advantage, pay out rates, etc;
- d) the licence holder is responsible for notifying the certified testing company and the Commission of any changes to their software so the software can be tested if required;
- e) the licence holder is responsible for providing any updated certificates to the Department;
- f) The Anti-Money Laundering Code also requires licence holders to report any suspicious transactions to the Financial Crime Unit.

The other important change that has occurred in the Isle of Man since 2001 is that the onus on deciding the territories from which wagers are to be accepted is now the responsibility of the operator and not the Isle of Man Government or the Gambling Control Commissioners. This means of dealing with the jurisdictional issue is in line with that taken by the United Kingdom Government.

The Isle of Man is up against stiff competition to attract such business, but it has considerable advantages over its competition because of the Island's state of the art telecommunications infrastructure and the geographical size of the Island which permits expansion of business which is not possible in other competing jurisdictions.

Another advantage the Isle of Man holds over its competition is the increasing wish of gambling companies to legitimise their businesses by launching them on, for example, the London Stock Exchange. In order for them to achieve this aim they need to be located in a premier, well-regulated jurisdiction like the Isle of Man.

Gambling Regulation

In order to ensure that the Isle of Man provides the most competent regulatory environment in the world for the on-line gambling industry, the Department has, through detailed world-wide consultation, produced a number of important documents which are considered by both regulators and the industry as ground breaking.

Application Procedure

The first aspect put in place relates to the application procedure for a licence, and in this connection a comprehensive application procedure was formulated based on the procedures used by the Gaming Board of Great Britain.

This procedure impressed the industry world wide because of its extensive nature and because the follow-up checks exceed those conducted by the strictest regulatory regimes in other jurisdictions. Checks include those on the applicant, parent and associated companies, the individuals involved in these entities (including checks on police records),

data protection compliance, customs, identification, involvement in professional organisations, personal banks and building societies accounts, etc.

Therefore in the first instance it is extremely difficult to obtain an Isle of Man licence. Indeed some entities have not proceeded based purely on the comprehensive nature of the application procedure.

Regulatory Regime

The second regulatory aspect relates to four sets of regulations to deal with systems verification, advertising, registration of accounts and prescribing descriptions of permitted games. These regulations are continually appraised and updated to ensure there is no weakening of the regulatory process as technological advances continue in this developing industry.

The prescribed regulations provide a list of games that are permitted under the Act to ensure that only games that can be strictly regulated are available on Isle of Man regulated sites.

The advertising regulations provide for the rules for advertising off and on a licensed website and include strict rules in relation to what has to be provided on the site and what is prohibited. The regulations also provide the Commissioners with powers of enforcement and penalties of up to £5,000 for each violation.

The Registration of Account Regulations provide for the rules and procedures that must be followed by the operator in registering new customer accounts. The Regulations also specify detailed rules on the way accounts must be managed, privacy of information on account holders and prescribe the penalty for contravention which is £5,000 for each violation.

The System Verification Regulations provide for the rules with which an operator must comply in conducting on-line gambling, provide certification of software and impose penalties for noncompliance of £5,000.

In relation to noncompliance with any Regulations made under the On-line Gambling Regulation Act, the Commission has the ultimate power to suspend or revoke the licence.

Anti-Money Laundering

The third regulatory aspect relates to the Anti-Money Laundering Code the Isle of Man has put in place which applies specifically to on-line gaming businesses. This Code eliminates the potential that such sites could be used for money laundering. The Code imposes requirements on on-line gambling businesses to establish anti-money laundering procedures, training and record keeping with failure to comply resulting in prosecution in relation to the breach. This Code is kept under constant review in compliance with the FATF principles.

Strict anti-money laundering procedures are required to be complied with which relate to identification of prospective customers, evidence of identity, changes to patterns of transactions, record keeping, records of transactions, retention of records, reporting suspicious transactions and training.

There is a legal requirement for licence holders to report any suspicious transactions to the Financial Crime Unit (“FCU”). These transactions are identified by software which is designed to highlight transactions on any account that for example, show that money has been deposited and few gaming transactions have taken place before it is withdrawn. The FCU will then investigate the report, check their data base, and if deemed necessary involve foreign jurisdictions in a staged approach to the investigation. In 2005 there were three cases where suspicious transactions, relating to gambling, were reported to the FCU. This information was passed to US law enforcement agencies.

The anti-money laundering processes, other regulatory requirements, and the strict application procedure ensure that those who would attempt to use such gambling sites in the Isle of Man for the purposes of laundering terrorist or other illegal funds are prevented from doing so.

Latest Additional Regulations

In addition, the Isle of Man has developed new Regulations to permit disaster recovery and the advertisement for off-Island on-line gambling sites as a means of attracting other business and building a level of expertise. Assistance is also being given to existing on-line companies that wish to re-locate to the Isle of Man through the introduction of transitional arrangement Regulations.

The Advertising Regulations provide that the promotion of gambling web sites elsewhere in the world have to comply with regulations on advertising to ensure they are not indecent or offensive, they are based on fact and they are not false, deceptive or misleading in any material particular.

The development of Regulations in the field of disaster recovery relate to the need for companies to have back-up facilities for on-line sites in well-regulated jurisdictions with excellent telecommunications systems. These sites are, as with all on-line gambling, subject to stringent regulation and licence requirements.

Gambling Forum

The Department of Home Affairs has continued regulatory development by setting the terms of reference for the On-line Gambling Forum. When established, this body will bring industry and Government together to work in partnership to provide an optimally regulated and commercially attractive on-line environment and avoid reputational risk. This body is seen world-wide as a model for providing a well-regulated environment for on-line gambling.

The Gambling Control Commission

The Isle of Man Gambling Control Commission (“the Commission”) is an independent corporate body, initially established as the Gaming Board of Control in 1962. Its members are appointed by the Council of Ministers. It is probably one of the oldest established gambling regulatory bodies in the world and is empowered to regulate the entire gambling industry in the Isle of Man, excluding the United Kingdom National Lottery. There are five Commissioners one of whom acts as Chairman who must be legally qualified, and all of whom are Isle of Man residents.

The Role of the Commission

The role of the Commission in relation to on-line gambling sites is to supervise on-line gambling operations and includes the following:

- a) To ensure that on-line gambling is fairly and properly conducted and ensure compliance with the provisions of the 2001 Act, the Regulations and licence conditions;
- b) To investigate the character and financial status of persons behind on-line gambling operations and to ensure that all fees payable to Treasury are duly paid and accounted for;
- c) To approve the company's Isle of Man resident "Designated Official" who must be a Director of the licence holder, and a person of integrity and competence. In addition the Commission considers the character and reputation of the Designated Official and their competence and experience in both IT and gambling;
- d) To ensure accounts are secure against invalid access and systems failure;
- e) To ensure the site is regulated, the licensee has a physical address, it has a regulator namely the Isle of Man Government, persons under the age of eighteen years are not permitted to play and that persons who do play have the assurance that their winnings are legally recoverable;
- f) To ensure advertisements are not indecent or offensive, are based on fact and are not false, deceptive or misleading. Additionally, advertisements must not have any sexual content or contain any material in breach of copyright. If the Commission is of the opinion there has been any breach of these standards it will direct the licensee to cancel the advertisement or to change it. Breach of these standards also constitutes an offence as does failure to comply with directions issued by the Commission;
- g) To ensure that the licence holder continues to supply current information;
- h) To undertake routine inspections and audits. In particular the Commission can order a licensee to remove a director or manager from office and can also direct that a particular person should not be appointed a director or manager;
- i) To enter premises to access records, documentary or otherwise, and computer programmes. It is an offence to obstruct entry and access to such records or to provide false or misleading information;
- j) To supervise the audit of sites. The Commission demands the co-operation of the licence holder and a full and unrestricted information flow which in all cases must be without prompting by the Commissioners. If a random audit reveals anything less than complete co-operation and a full and accurate information flow, licences are at risk of suspension or cancellation and the Commission may recommend prosecution to the relevant authorities;
- k) To suspend or cancel the licence if the Commission is satisfied that the licence holder was not eligible to have been granted a licence.

Resources of the Commission

The Commission has available to it specific technical advice from accountants and statisticians but may also obtain further advice when that is necessary. In addition a new senior Government official is shortly to be appointed entitled the "Director of Gambling Regulation" who will provide for oversight of the ongoing development of the regulation of the industry.

Future Development of the Gambling Control Commission

The ongoing need to put in place a more extensive body to oversee the regulation of the industry and to ensure there is no compromise in the regulatory mechanism has resulted in the enactment of the Gambling (Amendment) Act 2006. This Act will establish a regulatory body entitled the Gambling Supervision Commission which will have increased powers and responsibilities in relation to the industry, independent of Government in the same way as the FSC regulates financial institutions in the Island. The Act also adds a requirement that one member of the Commission must have experience of on-line business and another have experience of gambling business to ensure there is relevant expertise in the Commission.

The Gambling (Amendment) Act 2006

This Act establishes important new licensing objectives namely:

- a) ensuring that gambling products promoted by operators in the Island can compete effectively throughout the world;
- b) facilitating competition;
- c) facilitating the provision of modern products and services;
- d) ensuring that gambling is conducted in a fair and open way;
- e) protecting children and other vulnerable persons from being harmed or exploited by gambling; and
- f) preventing gambling from being a source of crime or disorder, being associated with crime or disorder or being used to support crime.

Underage Gambling

There are rules which are strictly enforced to ensure that persons under the age of 18 cannot gamble.

The process for opening an account is that an individual has to register, giving particulars of his age, identity and place of residence. The applicant must then deposit funds by means of a credit or debit card. Licence holders use various methods of age verification including large data base services such as Experian to ensure customers are not under

age. In addition in order to withdraw funds a pin number is issued by post by on-line gaming licence holders to the name and address provided at registration.

The Isle of Man Government works with licence holders to ensure that further restrictions will be put in place to prevent under age gambling.

Gambling Addiction and Problem Gamblers

The protection of the vulnerable is one of the Commission's core values and one which is taken very seriously. All holders of gambling licences in the Isle of Man are, as a matter of course, required to satisfy the Commission that they undertake and provide for a high-level of social responsibility in their specific gambling activities so as to ensure that should a particular player be recognised as displaying signs of addiction, there is immediate access to assistance.

Licence holders or applicants for licences are required to demonstrate their social responsibility procedures and to provide a link, or for terrestrial operations provide literature, or information and a contact number for a problem gambling agency. These procedures are audited on an ongoing basis.

The Commission is working with other International Regulators to continue to add to their current broad understanding of the international context of this problem and with local agencies in order to maintain best practices. This work will continue as, regrettably, there are jurisdictions which permit internet gambling without addiction deterrents.

There is a customised gambling site 'self-exclusion aid' for those who want to take immediate action themselves, which prevents their computer from accessing any on-line gaming site until they feel they are in control again.

It has been suggested by the Responsibility in Gambling Trust ("RIGT"), a major co-founder of the international referral portal for problem gamblers that on-line operators should be persuaded to donate to the Trust. The Isle of Man Government is supportive of this suggestion and intends to put in place licence conditions that will require Isle of Man licence holders to contribute to the provision of this service.

In addition the Gambling Control Commissioners at the Gambling Regulators European Forum Conference in 2005 requested information from participating member states relating to problem gambling :

- a) To ascertain what solutions other jurisdictions offer to problem gamblers and whether these solutions differ for 'local' and foreign operators and;
- b) To ask if there is an official or recommended help organisation which might be included on the web sites of internet gambling operations in their jurisdiction.

Benefits of the Isle of Man Regulatory System

- a) Prior to enactment of the Unlawful Internet Gambling Enforcement Act, a major proportion of bets placed by US citizens were with on-line casinos and sports book operations in poorly regulated jurisdictions. The Isle of Man provides an alternative to these off-shore locations by providing a strictly regulated jurisdiction which ensures operators have processes in place to prevent access from underage persons, deters problem gambling, deals with money laundering, provides legal redress for customers, provides player protection for monies owed and provides strict tests on software and pay out levels, etc.
- b) The Isle of Man wants to work with the United States to put in place any additional regulatory measures considered necessary.
- c) Terrorist organisations exploit any weakness in financial systems to launder funds. By insisting that on-line gambling business is carried out only in well-regulated jurisdictions, such organisations will be deterred from using on-line gambling operators to launder funds.
- d) The on-line gambling market is a worldwide business. It is likely that the number of on-line gambling businesses will reduce as the regulation of the industry becomes more comprehensive. Those businesses that succeed in this business environment may well choose to be listed on a stock exchange, and this will encourage the location of such business in well-regulated jurisdictions such as the Isle of Man.
- e) The Isle of Man believes, as with land-based gambling, on-line gambling is a well established recreational activity and therefore a regulatory environment must be provided in which it is safe to gamble on-line, ensuring the vulnerable are protected.

Conclusion

It is submitted that internet gambling in the Isle of Man is effectively regulated with the result that consumers and the payments system are indeed protected.