

**FEDERAL RESERVE BOARD AND TREASURY DEPARTMENT JOINTLY ISSUE
RULES TO PREVENT UNLAWFUL GAMBLING BY REGULATING THE
INSTITUTIONS THAT PERFORM THE RELATED FINANCIAL TRANSACTIONS**

New rules released jointly by the Federal Reserve Board and the U.S. Treasury Department (collectively, the “Agencies”)¹ require designated payment systems to establish and implement policies and procedures that prohibit those systems from facilitating, completing, or participating in transactions in connection with unlawful Internet gambling. The rules become effective on January 19, 2009 and require compliance by December 1, 2009. These rules implement key portions of the Unlawful Internet Gambling Enforcement Act of 2006 (“UIGEA”).²

Designated payment systems covered by the rules include automated clearing house systems, card systems, check collection systems, money transmitting businesses, and wire transfer systems. The rules require that entities with designated payment systems establish written, reasonably designed policies and procedures to identify and block “restricted transactions,” which involve the transfer of money to an “unlawful Internet gambling” website. As an example of reasonably designed policies and procedures for designated payment systems, the rules indicate that covered entities could choose to conduct due diligence at account opening in order to determine the risk of the commercial customer engaging in an Internet gambling business.

The new rules do not define “unlawful Internet gambling” beyond the definition used in UIGEA. UIGEA defines “unlawful Internet gambling” as “placing, receiving, or otherwise knowingly transmitting a bet or wager by any means which involves the use, at least in part, of the Internet where such bet or wager is unlawful under any applicable federal or state law in which the bet or wager is initiated, received, or otherwise made.”

The rules further provide that covered entities should monitor the Internet to detect unauthorized use of their designated payment systems, including trademarks. The Agencies noted that when unauthorized use of a trademark is discovered, the covered entity could take steps to seek the trademark’s removal from the gambling website, including legal action if available.

The rules also impose obligations on “third-party processors” of covered payment systems but a service provider simply providing “back-office support” to a depository institution is not a “third-party processor” under the rules.

¹ The new rules are available at this link:
<http://www.federalreserve.gov/newsevents/press/bcreg/bcreg20081112a1.pdf>.

² UIGEA prohibits gambling businesses from knowingly accepting payments in connection with unlawful Internet gambling and instructs the Agencies to identify and regulate designated payment systems to prohibit them from making those payments.

Moreover, not all payment services are covered under UIGEA. For example, check cashing and money order services conducted from a physical location are exempt, and the rules do not require gambling websites to block payments to their users and players (*i.e.*, to individual gamblers). The rules also exempt fantasy sports betting, subject to certain restrictions, including a requirement that rosters cannot be composed entirely of players from a single team and a prohibition on up-front prize declarations.

The Agencies' action came only a few days after House Financial Services Committee Chairman Barney Frank (D-Mass.) asked Treasury Secretary Henry Paulson to put a stop to issuing these regulations. In September 2008, Rep. Frank's Committee passed a bill requiring the Agencies to define the term "unlawful Internet gambling." The bill has not been approved by the full Congress.

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