

# Internet Gambling Regulation Compliance

BY STEPHEN KENNEALLY

**FOUR  
FOCUS  
POINTS  
FOR  
BANKS**



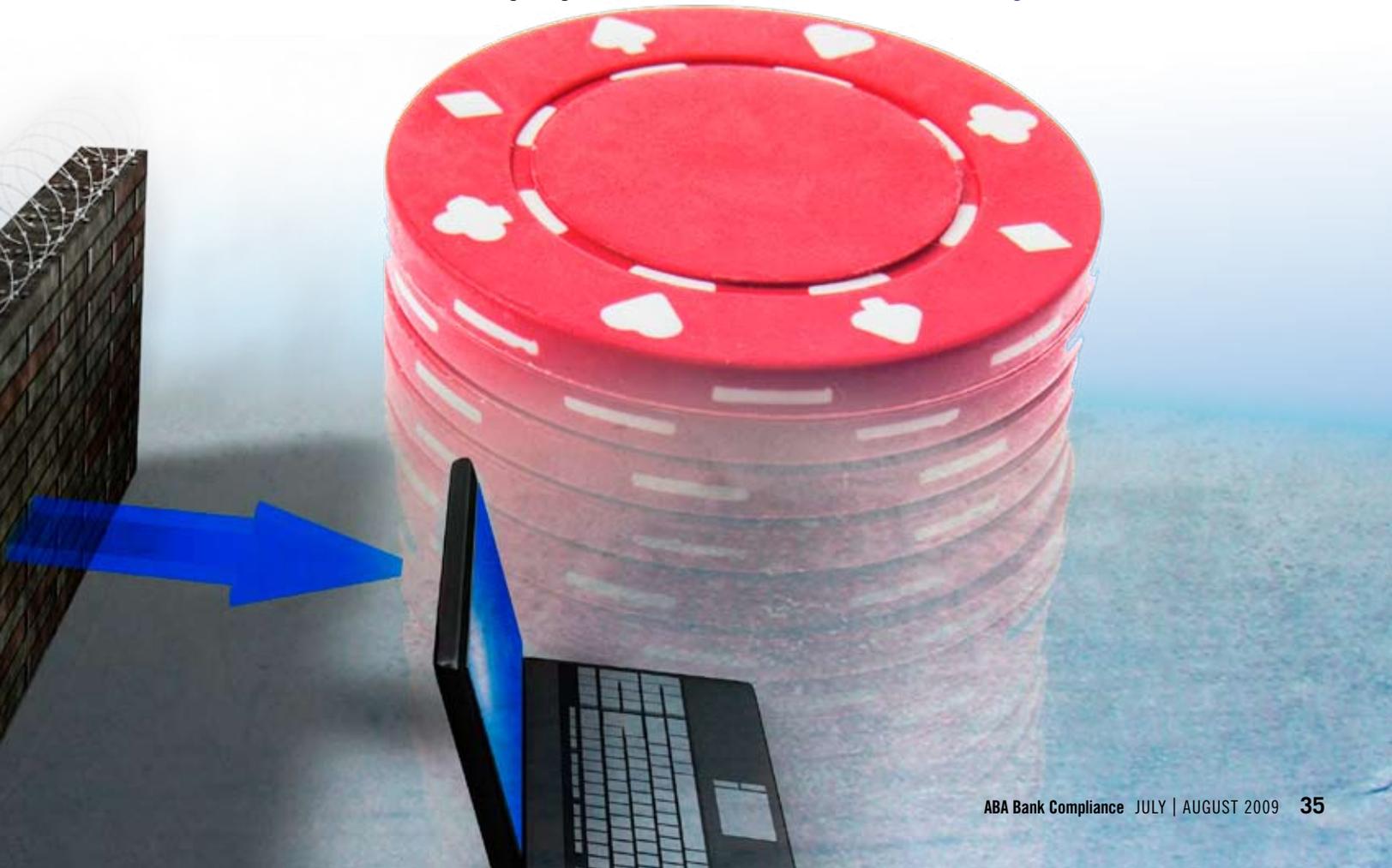
**THE UNLAWFUL INTERNET GAMBLING ENFORCEMENT ACT** (UIGEA) aims to limit on-line wagering by placing new prohibitions on banks making payments to Internet gambling businesses. The agencies responsible for writing the regulation and enforcing this broadly worded law, the Board of Governors of the Federal Reserve System and the Department of the Treasury, realized that a loose interpretation of the legislation enforced through its regulation would grind the payments system to a halt if each check, wire, ACH, and card transaction had to be validated as a lawful payment. Compounding this hurdle, the UIGEA did not define “unlawful Internet gambling,” leaving it to a patchwork of state and tribal laws.

Recognizing that it would not be practical to require banks from blocking payments they could not identify as unlawful, the final rule focuses on preventing unlawful Internet gambling businesses from benefitting from the payment system by denying them the opportunity to open bank accounts from which to receive payments. This indirect approach of requiring additional screening of commercial customers posing a risk of acting as unlawful Internet gambling businesses from opening bank accounts meets the UIGEA’s requirements, according to the regulation’s drafters. Financial institutions that have the direct customer relationship with commercial account holders bear the responsibility of introducing them into the payments systems.

With the exception of credit and debit card transactions, the final rule does not require poli-

cies and procedures specifically for blocking payment transactions. The final rule also mandates disclosures be made to commercial customers regarding the UIGEA’s restrictions.

The final rule has a few other key elements that banks must meet by December 1, 2009. Because this is a new final rule and the banking agencies have not completed examiner guidance, we don’t have the luxury of relying on historical data or experience to guide bank efforts. Based on research of the UIGEA and the rulemaking process in conjunction with dialogues with experts in the regulatory community we have identified four general areas where banks should focus their UIGEA efforts. A brief discussion of these topics follows and additional information can be found on ABA’s Web site at [www.aba.com/Compliance/UIGEA.htm](http://www.aba.com/Compliance/UIGEA.htm).





## The Four Keys to Bank UIGEA Compliance

- ① screening commercial customers at account opening
- ② policies and procedures to block prohibited transactions conducted via debit and credit cards
- ③ policies and procedures to follow when a commercial account processes restricted transactions
- ④ new notice requirements for commercial customers

### Additional Screening at Account Opening

The final rule attempts to prohibit unlawful Internet gambling businesses from receiving payments by preventing them from opening accounts in the first place. If they have no bank account, then they can't make or receive a payment. By December 1, 2009, banks must have written policies and procedures in place that demonstrate the steps they are taking to prevent a commercial entity acting as an online casino from opening an account. Most banks are meeting these requirements already under the "know your customer" (KYC) requirements, but they should formally incorporate the UIGEA requirements into their existing procedures in order to demonstrate compliance with the final rule.

When a new customer applies to open an account:

1. Determine whether the account is for an individual or a commercial entity. If it is for an individual no further action is required under the UIGEA final rule.
2. If it is a commercial entity, the bank, as part of its normal due diligence, should assess whether there is a "minimal risk" of it acting as an Internet gambling business. If so, then no further action is required under the UIGEA final rule.
3. If a bank is not able to determine if a commercial applicant has a "minimal risk" of acting as an Internet gambling business, they can rely on the applicant's own certification that they do not operate as an Internet gambling business.
4. If a bank determines that an applicant does operate an Internet gambling business, it can still open the account if additional standards are met including:
  - Requiring the applicant to provide evidence of their legal authority to offer online gaming. This evidence could be in the form of a state issued license or an attorney's legal opinion, and

- The commercial entity is required to provide a third-party certification that its Internet gambling business has controls in place to prevent improper use of the site by minors or from other individuals in other geographic locations where such gambling would be prohibited and the Internet gambling business must provide the bank regarding any changes in status of its legal authority to operate.

**Banks should** incorporate similar steps into their account opening procedures with a special focus on commercial account opening.

### Restricting Card Transactions

Banks will be obligated to establish written policies and procedures to block transactions financing wagers of unlawful Internet gambling that are made via credit and debit cards. It would be impractical for individual banks to be able to monitor and block suspicious individual transactions because of the volume and speed of card authorizations and the issuing bank's ignorance of the merchants involved. The final rule recognized this and allows banks that issue credit and debit cards to rely on policies and procedures developed by the card system operators (MasterCard, Visa, American Express, Discover, etc...) to block prohibited transactions.

The card system operators could meet their obligations by establishing a due diligence procedure reviewing merchants accepting debit or credit cards to determine if they are acting as Internet gambling businesses or they could develop a system of merchant and/or transactions codes for gambling payments that could be blocked. Although it is likely that some version of the "coding solution" will be implemented, the regulation is flexible and either of these approaches could be acceptable or even other models not provided as examples could prove adequate.

Banks will be required to have copies of the card system operators' policies and procedures that they will be relying upon in their possession by December 1, 2009. Banks will be allowed to rely on the card system operators' procedures regarding the UIGEA regulation. It is important to note that banks will not have to verify the effectiveness of the card system operators plans in order to meet the requirement. It is expected that federal regulators will review the effectiveness of the card network procedures. As of May 2009, the card system operators had not released their policies and procedures. It is anticipated that they will assign entities that offer online betting a merchant code that can be blocked.

It is not certain whether the card system operators will be differentiating between lawful and unlawful gambling when assigning these merchant codes.

**Banks should** contact their card networks to learn more about the policies and procedures that will be implemented and to obtain copies of those procedures well prior to December 1, 2009.

## Policies and Procedures When Restricted Transactions Are Known

Every financial institution that is a non-exempt participant must establish written policies and procedures describing remedial actions it will take if it discovers that a commercial account is processing restricted transactions. The final rule does not mandate any specific actions that must be taken, but relies on each participant to have established policies and procedures in place.

The final rule clarifies in \_\_\_6 *Non-exclusive examples of policies and procedures* the obligations that a non-exempt participant in a designated payment system must adhere to when it gains “actual knowledge” that a commercial account has processed restricted transactions.

According to the final rule, actual knowledge is gained when an entity knows or receives a report from a governmental entity such as a law enforcement or regulatory agency that a commercial account is processing restricted transactions. A financial institution that merely has suspicions of restricted transactions, but does not know for certain, is not obligated to initiate the policies and procedures.

When the “actual knowledge” threshold is met, the final rule does *not* provide participants with a set of standard actions to implement. The overview discussion notes that it will be left to the participants “business judgment” whether it is appropriate to deny the commercial customer access to a particular payment system or to close the account entirely or some other action. However, participants should understand that their regulators will be reviewing the written policies regarding remedial actions.

Banks should draft policies and procedures to follow when they receive “actual knowledge” a commercial account is conducting prohibited transactions. Bank actions could include, but are not limited to:

- Warning the customer
- Blocking the customer from using that particular payment system
- Closing the account
- Conducting additional due diligence on the commercial customer

**Banks should** establish policies and procedures outlining their proposed actions and they should ensure that the appropriate bank personnel have a clear understanding of the “actual knowledge” threshold.

## Commercial Account Notice

The final rule requires that banks communicate to their commercial customers that restricted transactions are prohibited under UIGEA. However, the regulation is flexible regarding how the communication is made. It could be made through a revised commercial account agreement for new customers, via a notice sent to established commercial customers, or possibly even through some other methods including even a notice on the bank’s web site as long as the commercial account holders are reasonably likely to receive it. Banks are not required to update account agreements or provide notice with a periodic statement to comply with this UIGEA requirement.

**Banks should** determine the appropriate model language and the vehicle for its delivery.

## What the Final Rule Does NOT Require

It is also very important to understand what the final rule does **NOT** require.

- Banks are not required to monitor payments in or out of their bank to determine if they are financing lawful or unlawful Internet wagers.
- Banks are not required to re-investigate the business models of existing commercial customers to assess their likelihood of accepting online wagers.
- Banks are not required to have written policies and procedures to block ACH, check, or wire payments related to Internet gambling.
- Banks are not required to allow payments for “lawful” gambling transactions, but can block or “over block” all transactions related to gambling if they choose, without additional liability.

Additional information on the regulation’s requirements and a list of frequently asked questions can be found [www.aba.com/Compliance/UIGEA.htm](http://www.aba.com/Compliance/UIGEA.htm). BC

## ABOUT THE AUTHOR

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