

Comparing the Maryland & NY gaming indictments

Some in the internet gaming industry may feel they barely had time to absorb the magnitude of the indictments made public by the Department of Justice, in Manhattan, in April, before federal authorities in Maryland jumped into the act. On 23 May, the US Attorney's Office for the District of Maryland announced indictments¹ against two enterprises and three individual defendants under the Illegal Gambling Business Act ('the Act')² and federal anti-money laundering laws³ - ten internet domain names were seized along with the contents of several international bank accounts. Stuart Hoegner, Managing Director of the Gaming Counsel Professional Corporation, analyses these indictments in light of similar ones in New York (NY) and discusses their implications.

The Act is a federal statute that requires an underlying state law violation in order to apply. Without a breach of state law, there is no breach of federal law under the Act. Here, the gambling business is alleged to violate Maryland law. The Maryland Code prohibits, among other things, betting and wagering and making or selling 'a book or pool on the result of a race, contest, or contingency'⁴. In the past, the current US Attorney in Maryland has taken the position that Texas Hold 'Em, when played for money on the internet and available to Maryland residents, violates §12-102 of the Maryland Code⁵. He has also used the Act, federal money laundering prohibitions and state law violations to seek and obtain

forfeiture of amounts in bank accounts associated with internet gambling⁶.

Comparing NY with Maryland

Much can be learned about the Maryland indictments by comparing them with the recently-unveiled indictments in the Southern District of NY⁷. The differences are more striking than the similarities. Start with the development of the cases in each state. The NY indictments are understood to have grown out of prior investigations involving Neteller Plc and Daniel Tzvetkoff, among others.

By contrast, the most damaging information obtained by the US Attorney's Office in Maryland appears to have come by means of an elaborate sting. In an affidavit in support of seizure warrants relating to the domain name and fund seizures⁸, a special agent with US Homeland Security Investigations outlines the role of Linwood Payment Solutions in the operation. Linwood was an undercover payment processing business established more than two years ago near Atlantic City. Linwood and the undercover agents behind it 'established a website on the internet, opened bank accounts, and set up a payment processing plant with a number of employees capable of handling thousands of transactions on a daily basis'⁹. The agents then purportedly had dealings with top managers of foreign gaming and betting operators to discuss business and negotiate processing contracts. According to the affiant, Linwood 'processed millions of dollars in transactions during the past two years for a number of internet gambling organizations including Absolute Poker, Ultimate Bet, BetEd, K23 Group Financial Services doing business as BMX Entertainment Limited, and

Nemesis Group doing business as Chargestream Ltd'¹⁰.

Interestingly, given the fact that the evidence gathered through Linwood includes materials regarding Absolute Poker and UB, those entities and their alleged principals were not named in the Maryland indictments. As interesting is the fact that the Maryland investigation had been going on for more than two years - far longer, at least, than any information provided by Mr. Tzvetkoff was in the hands of the NY prosecutors - but the Maryland indictments contain fewer counts on lesser charges.

Unlike NY, there are no allegations in the Maryland indictments that the defendants violated the Unlawful internet Gambling Enforcement Act (UIGEA)¹¹, or conspired to commit wire fraud¹² or bank fraud¹³, although the Homeland Security Special Agent does refer to the UIGEA and the Wire Act in the applicable statutes section of her affidavit. The bank and wire fraud conspiracy count against several of the NY defendants is the most serious pending charge; federal law provides for a maximum prison term on conviction of 30 years¹⁴. Without minimizing the seriousness of the Maryland charges - money laundering and illegal gambling have maximum possible federal prison terms of 20 years and five years, respectively - wire fraud and bank fraud are not on the table *ab initio*. The absence of bank or wire fraud-related counts in Maryland shows that federal prosecutors believe they can continue to make cases against foreign operators without the kind of deceit that is being alleged in NY. After 15 April, observers may have supposed that operators not engaging in bank fraud in the US would not be molested by the Department of Justice or that they

would perhaps see less harassment. Any such hope now appears to be misplaced. Even without wire or bank fraud counts, the Maryland defendants face serious illegal gambling and money laundering charges. This risk extends to many gaming and betting operators currently serving the US market.

State law

What can be said of the respective state law violations? In NY, the alleged criminal act is a class A misdemeanor pursuant to state law. The relevant section provides that '[a] person is guilty of promoting gambling in the second degree when he knowingly advances or profits from unlawful gambling activity'¹⁵. A person engages in 'gambling when he stakes or risks something of value upon the outcome of a contest of chance or a future contingent event not under his control or influence, upon an agreement or understanding that he will receive something of value in the event of a certain outcome'¹⁶. NY is a 'material element test' state, i.e., it examines 'the element of chance by determining whether a particular game contains chance as a material element affecting the outcome of the game'¹⁷.

The gambling offences in the Maryland Code are also classified as misdemeanors. Federal prosecutors in Maryland have submitted before that Maryland law 'does not explicitly define gambling or unlawful gambling'¹⁸. However, Maryland does not appear to be a 'predominance test' state, either¹⁹, that is, it may not be a state in which the question is whether skill or chance predominates in a particular game²⁰. Accordingly, it may be ambiguous whether the alleged state law violations in Maryland and NY favor one set of defendants over another. Neither state seems

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to lean towards the predominance test. Both states appear to accept that a game where chance does not predominate can still be gambling. However, the definition of 'gambling' in the NY penal law might be seen to tie 'gambling' more expressly to 'a contest of chance' than the Maryland Code does. This might not matter for counts tied to sports betting, as in Maryland, but to the extent that the NY indictments deal primarily with an assessment of poker under state law, federal prosecutors in New York may have a harder path ahead with the illegal gambling and the UIGEA counts. Naturally, prosecutors in both jurisdictions will make the case that all of the activities amount to violations pursuant to the laws of each state.

What is the business of gambling?

One of the indicted individuals in Maryland, David Parchomchuk, has claimed through his representatives that he is not and never has been an owner of ThrillX Systems Limited and that he has only 'provided technical consulting services' to ThrillX, among other clients. However, the indictment against Parchomchuk says nothing about these consulting services; it contains the blanket assertion that ThrillX, Parchomchuk, and Darren Wright, among other things, conducted and owned an illegal gambling business. The US Attorney in Maryland may believe he can establish that Parchomchuk had an enhanced level of involvement in the gambling business. As a factual matter, however, if Parchomchuk was only a software developer and did not conduct, manage, finance, own, or market 'www.beted.com', ThrillX, or affiliated vehicles, then this may represent a new front in the Department of Justice's war against internet gambling. To date, the

main targets of federal prosecutors have been operators, processors, marketers, and their principals. According to Jeff Ifrah, Parchomchuk's counsel in the Maryland case, '[b]y indicting a software programmer, Maryland has expanded the definition of who is 'in the business of' gambling. Traditionally, only operators, processors and their owner/directors have been included in this definition'. It remains to be seen how the facts will shape up to support the indictment of Parchomchuk and the other defendants.

Implications

Questions coming out of the 23 May Maryland announcement are:

- How do these indictments, on the heels of NY, affect the timing and form of any regulation of the internet gaming and betting sector in the US?
- What does this mean for the US market and for international operators?
- Will other states follow these examples?

The Maryland indictments may not provide much in the way of answers. In one sense, the May indictments may be another weight tipping the scale away from federal regulation of internet gaming. Irrespective of increasing support from the US land-based casino operators, it will likely be seen as increasingly bad optics to push a federal gaming initiative while major entities in the internet gambling industry are under indictment, including in Maryland. This argument gets more traction the closer we get to next November's US presidential and congressional elections. However, at the time of writing, Rep. Joe Barton (R-TX) has introduced H.R. 2366, the Internet Gambling Prohibition, Poker Consumer Protection, and Strengthening

UIGEA of 2011. This measure joins Bills recently introduced by Reps. Campbell (R-CA) and McDermott (D-WA).

In other respects, the cases in Maryland will not affect the debate. At the very least, they (partly) concern sports betting websites. Few people seriously believe that sports betting over the internet will be regulated by Congress and allowed to be offered in the United States any time soon; that was the case both before and after the Maryland indictments were announced. It is also difficult to discern how Maryland will impact the various intra-state gaming initiatives currently under consideration in the US. Several of the state initiatives are confined to online poker and state regulation proponents may not be too swayed by what's happening in Maryland. On the whole, the Maryland cases will not likely have much impact on this debate. (The suspension of Full Tilt Poker's gaming licences by the Alderney Gambling Control Commission on 29 June is likely to have more of an influence on the US regulation debate than the events in Maryland.)

While the actions in Maryland will continue to make things difficult for US-facing operators, and while it may drive some US players and bettors out of the market, it seems trite to say at this point that the prohibition course being pursued by the United States will not succeed in choking off the industry. Certain states might be blocked by some US-facing sites in an attempt to mitigate risk, but there will likely be operators willing to take US action regardless of how bad things get for them there. This will, in turn, continue to drive transactions away from more reputable operators to less reputable ones. European operators dealing in heavily regulated jurisdictions will continue to be

loath to have anything to do with this grey market. The Maryland prosecutions should not particularly affect the approach taken by other law enforcement agents in the US. In Maryland itself, these cases are just continuing a trend being pursued by the US Attorney there. It will not be surprising to see new action taken by the Department of Justice elsewhere in the US against participants in the internet gaming and betting sector; this is also part of a pattern and will continue regardless of the Maryland indictments. Observers should also not overlook state-level actions, either. States will not only cooperate with federal investigations; they will launch their own ventures to attack what they see as state law violations.

Even though the broader implications of the Maryland indictments may be limited, the comparisons with the NY prosecutions are instructive. It is perhaps too early to say whether the underlying purported state law violations will be easier to establish in one state or the other, but the use of the sting (Linwood), the absence of a bank fraud count, and the possible expansion to including a software developer as a defendant (if borne out by the facts), may signal that the Department of Justice will be even more aggressive in its internet gaming and betting prosecutions after the Manhattan indictments.

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1. Indictment, United States v ThrillX Systems, Ltd et al, Crim. No. CCB-11-0238 (D. Md., 2011); Indictment, United States v K23 Group Financial Services et al, Crim. No. CCB-11-0239 (D. Md., 2011).
2. 18 U.S.C. § 1955.
3. 18 U.S.C. § 1956.
4. Md. Code Ann., Criminal Law § 12-

102 (2011).

5. See Government's Rule 11 Memorandum, United States v Davitt, Crim. No. CCB-10-0751 (D. Md., 2010). This position was the basis for a plea agreement in the Davitt case: Plea Agreement, United States v Davitt, Crim. No. CCB-10-0751 (D. Md., 2010).

6. Complaint for Forfeiture, United States v Contents of Various Bank Accounts (Electracash et al), Civil No. 09-2937 (D. Md., 2010). See also Van Smith, 'Feds in Maryland Seize Six More Bank Accounts Tied to Laundering Gambling Proceeds', *Baltimore City Paper*, 24 September 2009, at <http://blogs.citypaper.com/index.php/2009/09/feds-in-maryland-seize-six-more-bank-accounts-tied-to-laundering-gambling-proceeds/>

7. Superseding Indictment, United States v Scheinberg et al, 10 Cr. 336 (S.D.N.Y., 2011). See also: Complaint, United States v PokerStars et al, 11 Civ. 2564 (S.D.N.Y., 2011); Post-Indictment Restraining Order, United States v Scheinberg et al, 10 Cr. 336 (S.D.N.Y., 2011); and, Arrest Warrant In Rem, United States v PokerStars et al, 11 Civ. 2564 (S.D.N.Y., 2011).

8. Affidavit in Support of Seizure Warrants, at www.regulatingonline.com/wp-content/uploads/2011/05/56092260-Linwood-SSW-Affidavit.pdf

9. Id. at 8.

10. Id.

11. 31 U.S.C. §§ 5361-5367.

12. 18 U.S.C. § 1343.

13. 18 U.S.C. § 1344.

14. This is only an expression of the maximum possible prison term under the United States Code. Many factors can affect sentencing.

15. N.Y. Penal Law § 225.05 (Consol. 2011).

16. Id. at 225.00.

17. Anthony N. Cabot, Glenn J. Light & Karl F. Rutledge, 'Alex Rodriguez, a Monkey, and the Game of Scrabble: The Hazard of Using Illogic to Define the Legality of Games of Mixed Chance and Skill', 57 *Drake L. Rev.* 101, 109 (2009).

18. Government's Rule 11 Memorandum, United States v Davitt, supra note 5 at 4.

19. *Brown v State*, 210 Md. 301, 307 (Md. 1956). In *Brown*, the Maryland Court of Appeals considered whether a pinball machine was an illegal gambling device. The Court construed the Maryland Code as follows: 'The insertion of money and the operation of a device by the player in a hope of winning a monetary reward in varying amounts... constitutes a bet or wager, regardless of the element of skill.'

20. See Cabot, Light & Rutledge, supra note 17 at 108.