Internet Gambling and the Canadian Conundrum

I. Introduction

The past ten years have been a time of great expansion in the Canadian gambling industry.¹ Provincial governments, which maintain primary control of gambling activities, have struggled to develop socially-acceptable policies to guide this expansion. Just as the casino and video gambling policies of the 1990s settle, and some of the public debate dissipates, the Internet gambling issue awaits. To date, Canadian federal and provincial governments have not enacted a new legal framework to deal with the emerging Internet gambling issue.² Two countries that Canadian policy makers are sure to have their eyes on are Australia and the United States, applicable jurisdictions because of their federal status. Australia serves as the example of state-managed liberalization by allowing Internet gambling to flourish within a strong regulatory framework. Conversely, federal policy-makers in the United States have focused on an outright ban of the activity.

This paper summarizes the Internet gambling policy options developing in Australia and the United States and places Canada's gambling framework within this context. In all three countries, individual state, territorial, or provincial governments have exercised licensing, regulation, and/or operational control over land-based gambling activities, as opposed to national government control. I will argue that Canadian policy-makers face unique challenges because of the degree of involvement provincial governments have practiced in land-based gambling activities.

A. What is Internet Gambling?

Internet gambling refers to the placing of real money bets using one's personal computer via the Internet. Three general types of Internet gambling sites exist: sports/event wagering, lottery ticket sales, and casino-game-style betting.³ It is the casino version of Internet gambling that perhaps draws the most public attention because of its high-quality graphics and virtual casino experiences offered.

Internet casino gambling emerged in its sophisticated form in 1995.⁴ The most recent figures estimate that by 2001, Internet gambling revenues could surpass ten billion dollars

1 See The Canadian Gambling Patchwork, (Calgary: Canada West Foundation, 1999).
2 In 1996 Liberal MP Dennis Mills introduced Private Member's Bill C-353, An Act to Amend the Criminal Code of Canada (the regulation of internet casinos) in November 1996. The Bill was not sponsored by the governing party and did not pass second reading. No provincial government has legislated regarding Internet gambling to date. See British Columbia, White Paper on Gaming Legislation: Gaming Legislation and Regulation in British Columbia (Victoria: Gaming Project Working Group, 1999) at 241.
3 National government refers to the “Federal Government” in the United States and Canada and “the Commonwealth” in Australia.
(U.S.) world-wide. While there are no conclusive statistics regarding the number of users, what is known is the sustained growth of Internet gambling sites available to Internet surfers. It is estimated that more than two hundred and eighty websites that provide opportunities to gamble on the Internet exist. 

The possibility of Internet gambling poses at least four issues for policy-makers in federal states:

1. If Internet gambling is desirable, how should it be developed? If it is not, how should it be controlled?
2. Which level of government is better positioned to regulate or control the activity? Further, is it possible to place “controls” on Internet gambling sites, such as to enforce any regulation imposed by governments?
3. In the “borderless” Internet, how can governments generate revenue from gambling activities?
4. What kind of social costs are involved in Internet gambling?

This paper highlights some available policy options stemming from the above issues. There is less of an emphasis on the social costs of Internet gambling; however, this topic has formed the basis for a great number of government and academic studies and reports.

B. Where are Internet Gambling Sites Located?

Uncertainty in North America surrounding the legality of Internet gambling has led to the creation of several “safe-havens” for Internet gambling service providers in many Caribbean countries. In some of these havens, such as Antigua, systems for licensing have been established. Typically, the licensing procedures established in the “haven” countries require minimal effort and cost.

As well, a number of Internet casinos operate out of five Australian states and territories. These sites offer gambling opportunities to users worldwide. As explained below, some Australian states and territories have introduced licensing programs that, arguably, provide more security than the “haven” countries.

6 United States, National Gambling Impact Study (Washington: National Gambling Impact Study Commission, 1999) at 5-1; hereinafter cited as “NGIS.” There is no consistent measurement of the total revenues because of the newness of the industry. Also see note 4 at 17.11 for more estimates.
8 For example, the NGIS and the Productivity Commission Report are the most recent compilations of government consideration of the gambling issue generally. In the Canadian context, consider annual reporting of the Nova Scotia Alcohol and Gaming Authority and the recent B.C. White Paper (see note 2). As well, the Canada West Foundation has put forward a number of reports concerning the social costs of gambling in general. See Canada West Foundation home page. Found at http://www.cwf.ca.
9 See note 4 at 17.5.
10 See above.
11 See above at 17.5 and 17.6.
II. The Canadian Legal Framework Applied to Internet Gambling

It is first necessary to understand the basic framework for legal gambling in Canada. The power to legislate in relation to matters of criminal law is constitutionally assigned to the federal government in section 91(27). It has been held that sections 92(7) and 92(13) of the Constitution Act, 1867—provincial jurisdiction over the administration of charities and over property and civil rights—grant authority to provinces to legislate and regulate those gambling activities. The current gambling provisions were added to the Criminal Code of Canada in 1969, at which time electronic forms of gambling were not explicitly contemplated. In 1985 the Code was amended to address electronic forms of gambling and to hand sole responsibility over it to provincial governments.

The Code creates a number of gambling offences. As an example, consider section 206(1)(b) of the Code, which makes it illegal to operate or participate in any games of chance or lottery schemes. The section states:

Everyone is guilty of an indictable offence and liable to imprisonment for a term not exceeding two years who sells, barters, exchanges or otherwise disposes of, or causes or procures, or aids or assists in, the sale, barter, exchange or other disposal of, or offers for sale, barter or exchange, any lot, card, ticket or other means or device for advancing, lending, giving, selling or otherwise disposing of any property by lots, tickets or any mode of chance whatever. [Emphasis added.]

Operators are subjected to harsher penalties than players; section 206(4) states that anyone who “buys, takes or receives a lot, ticket or other device mentioned in subsection (1) is guilty of an offence punishable on summary conviction.” Based on these provisions, it is likely illegal for a Canadian resident to gamble on the Internet in their own home. Note, however, that if section 206 were the only lottery scheme provision in the Code, most lottery schemes would be illegal.

Many gambling activities are permitted in Canada because of section 207 of the Code, which creates exceptions to the overall ban. Section 207(1)(a) permits “lottery schemes” that are “conducted and managed” by provincial governments. A second exception is carved out for provincially licensed lottery schemes conducted by charitable organizations, exhibition associations, and in certain circumstances, private individuals (sections 207(1)(b-d)).

According to section 207(4)(c), lottery schemes “operated on or through a computer, video device or slot machine” are not permitted unless they are conducted and managed under the exception in section 207(1)(a) — the provincial government exception. Given section 207(4)(c), and the reality that gambling profitability has been highest in the area of machine gambling, several provincial governments have become involved in the provision of machine gambling activities such as slot machines and video lottery terminals. Under the current framework, Internet gambling would likely fall under section 207(4)(c), and would therefore only be legal if conducted and managed by a provincial government.

A. The Canadian Conundrum

There exists a fundamental distinction between the Canadian model of gambling
control and the American and Australian models. In Australia and the United States, state and territory governments generate revenue from gambling indirectly through taxation. In Canada, regulated gambling activities benefit charitable organizations, exhibition associations, and provincial governments via direct revenue streams. Therefore, for those activities that are provincially “conducted and managed,” the lottery schemes are — at some level — managed by provincial governments. There is little room in the Canadian framework for privately-operated, commercial lottery schemes.

The conduct and management of provincial government gambling operations is distinct from provincial government regulation of gambling activities. Regulation refers to licensing and encouraging compliance with gambling regulations. In Canada, the same government often performs these two tasks. For conduct and management purposes, provincial governments either contract with private companies to deliver gambling activities such as casinos, lotteries, and video lottery terminals (VLTs), or they directly operate such lottery schemes. At all times, the provincial government must be the “operating mind” of the lottery scheme.18

The exclusive control exercised by Canadian provinces in the area of lottery schemes is deliberate. Provinces began to lobby for the elimination of federal involvement in lottery schemes in 1979 and were successful in removing this possibility in 1985. There is no indication that provincial governments would be interested in diminishing this control — and its accompanying revenue streams — for the area of Internet lottery schemes. Canadian provinces have devoted considerable energy to establishing unique, locally-responsive frameworks for land-based gambling. In some cases, provincial governments have been particularly alive to local public opinion, with some going so far as to require plebiscite before gambling expansion.19 In light of the energy spent to develop provincially-unique gambling policies, it would not be surprising if Canadian provincial governments sheltered against federal government involvement in either the conduct and management or the licensing of Internet lottery schemes.

B. Proposed Legislation

Although no province has enacted legislation to alter the current legal framework for Internet gambling, there has been some activity in Parliament, in the form of a private member’s bill, not supported by the Government. In 1997 MP Dennis Mills introduced Bill C-353, An Act to Amend the Criminal Code (Internet Lotteries).20 Although this Bill died on the order paper of the 35th Parliament, it is worth noting because it proposed a radical change. Bill C-353 proposed to enable either the federal or provincial governments to license private Internet gambling operators and to implement a taxation scheme — a major departure from the current framework in Canada. The minimal debate that occurred in the House of Commons upon first reading of the Bill did not examine the unique suggestion to legalize large-scale, privately-operated lottery schemes and to then tax earnings; nor did the discussion get into any detail about a potential amendment to the Code to introduce federal government licensing of games of chance.21
C. Summary

Under the existing Code framework, if there is to be legal Internet gambling in Canada it must be conducted by provincial governments. To date, there are no provincially-operated Internet casinos.

III. Australia as an industry front-runner

Australia permits land-based gambling activities through private operators with state or territory\(^{22}\) regulation. State and territorial governments are involved in regulating and taxing land-based gambling activities, such as casinos. In Australia, there are no publicly-managed gambling activities.

In some Australian states, the development of a comprehensive Internet gambling regulatory scheme has been fuelled by a desire to maintain state and territory control over gambling, and to position Australia as an international leader in the field.\(^{23}\) As a result, Australian state and territorial regulatory frameworks serve as apt experimentation models for other federal states.

In May 1996, the State and Territory Gaming and Racing Ministers came together to develop a *Draft Regulatory Control Model For New Forms of Interactive Home Gambling*\(^ {24}\) (hereinafter the *Draft Model*). The *Draft Model* argues that, “[p]rovided all States and Territories participate in the Model, the assistance of Federal bodies is unnecessary to provide effective regulation of interactive home gambling products sourced from within Australia.”\(^ {25}\) The *Draft Model* proposes that each state and territory develops consistent legislation to establish licensing and regulation standards for Internet gambling outside the purview of any Commonwealth body. Licensing systems would be established and adequate player protection would be encouraged. A taxation system that applies taxes based on the location of the gambler would also be established.

Since the release of the *Draft Model*, two states and two territories have implemented Internet gambling legislation: Queensland, Northern Territory, the Australian Capital Territory and Tasmania. In general, recent new state legislation has fallen in line with the *Draft Model*.\(^ {26}\)

As the states and territories of Australia assert their control over gambling regulation, it is not clear that the Commonwealth government is content to stay out of the field. In July 1999 the Productivity Commission of the Australian Commonwealth Government issued *A Draft Report on Australian Gambling*, (hereinafter “Productivity Commission Report”) with an extensive section regarding Internet gambling. The Productivity Commission Report’s authors state, [existing policy measures by individual States and Territories represent pragmatic responses to the rapidly evolving opportunities and threats posed by online and interactive gambling. They do not necessarily represent the optimal policy response.\(^ {27}\)

At the very minimum, the Productivity Commission Report suggests that it is more sensible to “take a national approach” to the regulation of Internet gambling. The international quality of Internet gambling and the technological complexity of the issue keeps this debate alive. Authors of the Productivity Commission Report suggest that, “[o]ne reason why regulatory

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\(^{22}\) In Australia, as in Canada, there exist both states (equivalent to Canadian provinces) and territories (equivalent to Canadian territories), which are distinct from the national government known as the Commonwealth (equivalent to the Canadian “Federal Government”).


\(^{25}\) See above.

\(^{26}\) See note 4 at 17.39 – 17.40. Tasmania’s legislation departs most freely from the suggested model, but for an example of legislation that aligns most closely with the *Draft Model*, see the *Interactive Gambling (Player Protection) Act, 1998*, enacted in the state of Queensland.

\(^{27}\) See note 4 at 17.44.
frameworks for Internet gambling tend to depart from principles adopted in other gambling modes is that regulators are aware of the profound difficulties of implementing a similar framework for the essentially anarchic internet. Further, commentators have been skeptical about the plausibility of the Australian states and territories to self-regulate in the Internet gambling field without dissent.

IV. The United States: A Nation-wide Ban

The problem presented in Australia may be bypassed in the United States, where policymakers have demonstrated increasing momentum to introduce a nationwide ban on most forms of Internet gambling. In the United States, gambling is regulated uniquely by each state. In all but two states, forms of gambling exist. Similarly to Australia, gambling revenues typically benefit state governments via taxation, with the states acting as regulators.

Existing federal legislation has been applied by some states to make the establishment of Internet gambling sites illegal for American citizens. In fact, the Federal Department of Justice has stated that existing federal law makes Internet gambling illegal. While the Department of Justice has made no commitment to prosecute these offences under the current provisions, movements are afoot to unify and strengthen the American position on Internet gambling. Based on two significant developments, it appears as though the influential wisdom in the United States favours a shifting of control to the federal government for Internet gambling, with the introduction of a nationwide ban.

The first development began in 1997 when Senator Jon Kyl introduced the Internet Gambling Prohibition Act (hereinafter the “IGPA”). The original IGPA died on the Senate floor, but a revamped IGPA was introduced in 1999. The Senate unanimously passed the latest version on November 19, 1999 and a companion bill is currently before the House of Representatives. The IGPA of 1999 amends the Federal Criminal Code to make it illegal for companies to establish online gambling venues. The Act exempts from penalty some forms of Internet gambling such as state lottery sales and authorized horse race betting.

The second development began in 1996 when Congress commissioned the National Gambling Impact Study (hereinafter “NGIS”). In July 1999 the NGIS Final Report was released. The first formal recommendation of the study states that “...states are best-equipped to regulate gambling within their own borders with two exceptions—tribal and internet gambling.” [Emphasis added].

The NGIS recommends that Internet gambling regulation takes a form similar to what was set out in the IGPA:

the federal government should prohibit, without allowing new exemptions or the expansion of existing federal exemptions to other jurisdictions, Internet gambling not already authorized within the United States or among parties in the United States and any foreign jurisdiction.

The Commission would charge federal bodies with the responsibility of developing control mechanisms to deal with infractions. “Because it crosses state lines, it is difficult for states to adequately monitor and regulate such gambling.”

28 See above at 17.5.
29 See note 23.
30 See the NGIS, note 6 for a complete discussion of the gambling framework in the United States.
32 NGIS, see note 6 at 5-7. Goldstein, see above at 18.
37 Recommendation 3-1 of the NGIS, see note 6.
38 Recommendation 5.1 of the NGIS, see note 6 at 5-12.
39 See above.
A. The Reaction

Much of the American literature regarding Internet gambling has focused on the introduction of Senator Kyl’s original Bill. In light of the NGIS recommendations, passage of the 1999 version seems likely. However, several criticisms have been raised.

One author criticizes the original Bill for its dismantling of state-control over gambling regulation. She states, “[t]he better approach would be a recognition of the long-held federal position that gambling should be permitted to exist in those states whose citizens choose to have it.”40 Another significant problem is enforcement. “While the IGPA would deter companies from locating their Internet gambling operations within the United States, Internet gambling would still flourish, as companies would simply base their businesses in countries with more hospitable gambling laws.”41

Law Professor Jack Goldsmith has provided an alternative view regarding the plausibility of enforcement. He argues that criticism based on the perceived efficacy of regulatory legislation should not factor into the policy debate, and enumerates various avenues the federal government can take to bolster a regulatory program dealing with the Internet. “The United States can achieve a great deal of regulatory control over these trans-jurisdictional communities by regulating these local persons and property.”42 Goldsmith argues that regulation of Internet gambling, like all other variations of government regulation, can be achieved when the harms produced by the activity outweigh the costs of the regulation.43

B. Summary

Presently, legislative initiatives suggest that the United States is headed for an outright prohibition of Internet gambling. The difficulty of regulation has caused legislators and commentators to look to the federal level of government to enter uncharted territory and to regulate an aspect of gambling.

V. Canada in Context

In both the United States and Australia, legislators are grappling with the issue of which level of government should regulate Internet gambling. In Canada, the key issue will be whether Internet gambling is desirable as a government policy option. While this policy debate has yet to unfold in Canada, the issue is certain to arise as Internet gambling options become increasingly available.

Under the current framework, provincial governments have the authority to introduce legal Internet lottery schemes in Canada. Due to the highly political response to gambling expansion of the past ten years, provincial governments may be reticent to enter the Internet gambling industry. This reticence will likely be due to concerns about the increasing accessibility of gambling.

The requirement that provincial governments conduct and manage electronic lottery schemes raises a plethora of policy issues including:

(i) Is it appropriate that a government operate Internet gambling sites?

(ii) How does a government’s dual role as operator and regulator affect the integrity of the latter role?
The above questions can, of course, be raised in regard to the treatment of land-based gambling. For example, is it appropriate that a government operates a land-based casino? In several provinces the answer has clearly been, “yes,” that it is appropriate for provincial governments to provide casino entertainment services. While it may seem incidental that a government is operating a land-based casino, is the perception the same if it is on the Internet? I submit that the Internet gambling industry sharpens the government gambling issue. As a policy option, it is less appropriate for a government to offer entertainment services, imbued with social costs such as addiction, in a medium that is infinitely accessible.

Provincial governments may find that citizens have a higher comfort level for some forms of Internet gambling. While on-line lottery ticket sales may seem appropriate, full-fledged Internet casinos may not. It will be the task of the policy maker to gauge public opinion in this respect.

There is another concern about government-operated gambling that the Internet gambling issue brings to the fore. Provincial governments have become reliant on revenues from land-based gambling activities. If Internet gambling options chip away at the established government industry, governments will be required to respond to protect existing revenues. If Internet gambling is not a desired policy option their hands will be tied. As this minor example illustrates, it may be that in times of greater diversity of gambling options, provinces-as-operators are no longer the most appropriate vehicles to deliver gambling services.

VI. Conclusion

The public debate about Internet gambling has not yet emerged in Canada. In Australia and the United States two distinct policy options are being tested. Australian states and territories have taken a preemptive strike against federal involvement in regulation. American legislators propose sweeping legislation that will remove state jurisdiction for certain forms of Internet gambling. It is not clear whether the Canadian Parliament, or provincial legislatures, will deem it necessary to alter the current Code framework. I predict that the increased level of accessibility that accompanies the Internet gambling industry will cause Canadians to question the appropriateness of a government-as-operator model. The current Canadian framework may not be the most appropriate model for Canada to take advantage of — or to manage the social costs of — the lucrative Internet gambling industry.