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July 21, 2010, Written Testimony of Michael K. Fagan

To the Honorable Barney Frank, Chairman, U.S. House Financial Services Committee, and the Honorable Members and staff of the Committee:

As a private citizen having probably-unique and specialized experience, background, and training concerning the issues raised by Internet gambling, I am pleased to submit testimony in this Committee's hearing entitled "H.R. 2267, Internet Gambling Regulation, Consumer Protection, and Enforcement Act." The Committee's time constraints may limit the details I might otherwise be able to provide on this issue; however, via the contact information on the letterhead of this document I remain available to the Committee for further consultation and/or expansion of these remarks.

By way of my background, I have attached at the end of this document a "biographic blurb" which at times has been used when I have given speeches or conducted training. In sum, I served my state and nation for approximately thirty years as a prosecutor of felons, including money-launderers and racketeers, with the greatest portion (25 years) of that time being an Assistant U.S. Attorney for the Eastern District of Missouri. Post-9/11, I was selected to head our District's anti-terrorism efforts and did so for six-and-a-half years, learning about and overseeing investigations concerning terrorist financing methods. Presently, I do consulting/advisory work for, and train, governmental bodies and corporations on a wide variety of topics, as described on my letterhead, above. I am neither a Democrat nor a Republican, but an apolitical independent (with a small "i").

As the career federal prosecutor once responsible, with surely-more-talented others, for the most, and the most successful, enterprise-based prosecutions and forfeitures of illegal unregulated commercial Internet gambling enterprises, their operators, and their facilitators, I have thought long and hard about the costs and benefits associated with Internet gambling. As I would sometimes tell cooperating criminal-witnesses in such investigations, I would have prosecuted people for failing to gamble, if the law required people to wager; thus, my chief interest in the topic was (and is) not based on some religious, moral, or philosophical attitude against gambling but, instead, on compliance with law. I do not disregard such attitudes, of course, just as I do not disregard the attitudes that argue in favor of legalization, regulation, and taxation of Internet gambling. Instead, I weigh those attitudes and the supporting evidence in order to arrive at a sound policy position. In sum, (1) having familiarity with the polar extremes (and the in-betweens) of attitudes on this issue, (2) having "inside" and lengthy experience with Internet gambling as it been practiced in the U.S. and elsewhere for the past

approximately-fifteen years, and (3) no longer having to limit myself to advocating for the Department of Justice's views, I am absolutely convinced that any action, however well-intentioned, by this Committee or by Congress, which would enable the expansion of Internet gambling in the United States will prove **far** more costly than maintaining the status quo. Moreover, it would be irresponsible to take any steps toward expanding the availability of Internet gambling—*i.e.*, giving up on controlling the problem-- in the United States before first directing and funding the Department of Justice and/or the states' Attorneys General to enable a coordinated, systematic approach to enforcing existing laws prohibiting and taxing such conduct.

My office and I advocated for a task force-type coordinated approach back in 1996-97, when these illegal offshore gambling enterprises first made their business appearance, via the Internet, in our citizen's homes and offices. Unfortunately, and contrary to our written suggestion, the then-management of the Department of Justice adopted a policy of letting these cases "percolate up from the field," rather than to address the issue comprehensively. This unfocused approach, in my view, contributed to the rapid growth in the number of offshore, U.S.-facing Internet gambling enterprises from approximately forty (at the time we urged creation of a task force) to, eventually, over two-thousand. Law enforcement and taxing authorities have yet to recover from the failure to adequately address the problem, which failure is all the more puzzling when, in my experience, these investigations easily "pay for themselves," in the sense that the recoveries available via fines, forfeitures, and back taxes (particularly with available interest and penalties) **far** exceed the costs of investigation, prosecution, and incarceration.

In my experience, these criminal gambling enterprises were frequently operated by and staffed with "corners-cutters" and sharp operators who, if they were not already associated with organized crime groups, were prone to mimic them, assist them, and/or adopt their ways. Many, of course, were charming or bright-enough characters—referring to them as "Runyon-esqe" is, perhaps, a nice way to paper over these characters' lack of character—but, the deeper an investigation would go into these operations, we could count upon finding additional criminality or, at least, the unpleasant scent of corruption, misconduct, and predatory behavior. Clichéd-behavior from old gangland movies came to life, as we came across or learned of outright fraud, threats and "leg-breaker" tactics, loan-sharking, point-shaving, and cash payments to college athletes or their family members to steer athletes to certain agents/programs, not to mention instances of more modern day criminality like illegal drug use/distribution, operation of illegal online pharmacies, extremely-sophisticated money-laundering and tax evasion, and terrorist financing opportunities. Commercial Internet gambling creates huge pools of capital, which effectively serve as wholly unregulated banks, inviting and facilitating money laundering and terrorist financing. These negatives I've listed do not include the significant social costs imposed by commercial gambling (legalized or otherwise—and I will let others address these social costs), but in my view the listed negatives, alone, outweigh the supposed "plusses" of gambling: the entertainment-value, or fun, of gambling made extraordinarily-convenient via the Internet, added to the necessarily limited and usually-remote chance of financial gain to the players, and the possible financial gain to the government via taxation (offset, of course, by the costs of regulation,

administration, and enforcement, and by lost taxes from other forms of entertainment and by product and service sales hurt by gambling, and limited by the “black market” gambling operations that will surely exist outside the regulatory framework—and which will thrive because of it). The claim that perhaps \$43 billion dollars in new tax revenues will result in 10 years’ time from legalizing and taxing this conduct rests upon assumptions both unsustainable and without basis in fact. States and tribes *will* opt out of a legalization regime, both because the conduct is unwelcome and corrosive and because it is certain to cost far more jobs—skilled and otherwise--in the “bricks-and-mortar” casino industry than online gambling creates. In that sense, H.R. 2267 promises buyer’s remorse. (Relatedly, this nation has plenty to be remorseful about given its history of mistreatment of Native Americans, and to legalize of Internet gambling--which will undercut the jobs and income presently available to Native Americans in the licensed, well-regulated real-world casinos they have built, invested in, and operated—simply constitutes rubbing salt in centuries-old wounds.)

This is all the more so because the bill under consideration does not require every aspect of an Internet gambling enterprise to be located, physically, within the United States. How can one reasonably assert that every non-U.S.-based aspect of such enterprises will be subject to effective federal regulation? How naïve to treat gambling like an industry where global outsourcing may be appropriate, given the well-established historical risks of corruption, dishonesty, and fraud attendant to commercial gambling. Neither does the bill mandate adequate initial and on-going background checks and certifications for all gambling enterprise employees nor of the gambling equipment/software /suppliers they utilize. The “let’s-legalize-this-now-and-worry-about-integrity-later” aura that surrounds this bill may have been unintended, but it could not be more plain. The aura may be attributable to the moneyed interests supporting the bill, since the much of that lobbying money likely comes from recent or ongoing multiple violations, by foreign companies (often controlled by U.S. persons), of existing federal law prohibiting online wagering. Legalizing Internet gambling without barring those who have made millions from purposeful and long-term disregard of federal and state laws simply rewards organized crime—yet another shortcoming of the proposed enactment.

Of course, one can argue that the negatives I’ve listed would disappear or diminish with legalization, regulation, and taxation. People engage in fairy-land arguments and wishful thinking like this with respect to a multitude of what are commonly called vices, whether advocating for increased opportunities for gambling or for narcotics use or prostitution, for business monopolies, unlimited political cash contributions, or any of a host of behaviors proven, by historical experience, prone to large-scale misuse and unmanageable by regulation at a reasonable cost. Internet gambling falls squarely within these latter categories. Further, H.R. 2267 provides little hope for effective regulation: it’s simply a bad bet to leave regulatory rule-making up to unelected Treasury Department officials who, unlike state authorities, have little or no experience in gambling regulation and who will be prone to the undue influence attempts that invariably accompany commercial gambling. Moreover, continued prohibition of Internet gambling hardly impinges on anyone’s freedom, as a practical matter, since the underlying conduct (gambling) remains highly available to individuals in more socially-

acceptable, safer contexts (such as card games and bets made with family or friends, in office “pools,” in regulated charitable settings, and via local or state-regulated casinos/lotteries). There is no shortage of opportunity for those in the U.S. who wish to recreationally gamble to do so, and to do so without the added costs imposed by the bookmaker/“house”/middleman necessarily present in Internet gambling enterprises.

Among these costs, apart from the “vigorish,” is that the gambling operator has every incentive to promote increased and unthinking gambling activity by consumers. History and recent exposes show that these incentives quickly lead to predatory behavior by the operator—including, *e.g.*, undisclosed odds manipulation and crass exploitation of electronic slot machine users; development by gambling software marketers of artificial intelligence to fool online poker-players into thinking they are competing with humans when, in fact, they are playing against computers controlling the outcome; so-called poker “education” websites fronting for and/or linking to illegal offshore gambling enterprises; tout services selling fraudulent supposedly-“inside” information and steering callers to certain sportsbooks without disclosure of financial inter-relationships; gambling operators setting up phony “independent” trade associations to act as supposed “watchdogs” or dispute-resolution services; and bribery abroad of supposed regulators or government leaders. Gambling software developers promise to create games available over the Internet that will match the crack-like addictive dopamine-stimulating modern slot machines – and any parent who’s puzzled or despaired over their child’s trance-like playing of video games during the past twenty years can readily see why Internet gambling operators are drooling over the chance to legally expand their market-base into the United States. Moreover, the conversion of existing points-based computer games into wagering-based games merely awaits enactment of H.R. 2267. Online gambling will go fast and far beyond poker.

At least responsible bricks-and-mortar casino operators can look a gambler in the eye and make the human assessment of whether he’s too drunk, mentally unhinged, despondent and desperate, developmentally disabled, or otherwise at a point at which it’s simply unfair to take advantage of him any longer. Internet gambling operators not only *cannot* assess these characteristics among their clientele, in my experience *they don’t care to*, preferring to prey on the weak and the strong equally. These, and more, indicia of the raw institutional greed intertwined with Internet gambling made unsurprising appearances in the many investigations and prosecutions with which I have personal experience. It seems cruel, in a nation with as many alcoholics and chemical-dependant persons as ours, to put them—and everyone else—at further risk of ruin by enabling them to gamble away their financial security at their home, office, library, and coffee-shop computers—and, now, through their hand-held devices: suddenly, “smart phones” don’t seem so very smart when you’ve lost your family’s grocery money on one. Problem and pathological gamblers affect far more than just themselves; they create networks of misery.

Moreover, a government that becomes dependent, even in a small way, upon tax revenue from gambling activities soon becomes prone to encourage gambling. As I noted above, I am agnostic about gambling, but I am also realistic enough to recognize that if my government is going to systematically encourage a behavior, it ought to be a behavior

that is more productive and less prone to exploitation. Further, in the United States the acceptability, or not, of commercial gambling has always been a local issue. Ignoring or carelessly jettisoning history seldom promises success. No persuasive policy reason suggests itself which would warrant the federal government taking this historical freedom-to-decide from local citizens. Experience proves that, once authorized on a national scale, Internet gambling operators would advertise and market their businesses to such an extent that no one in the United States would be immune from their messages. These messages, of course, would be calculated and likely to make long-term changes in Americans' behavior. Already, we are subjected to such messages in much of the country regarding existing legal gambling; indeed, we have allowed such without any prior study of how both the messages and the gambling are, for example, changing Americans' attitudes and productivity. To allow legalization of Internet gambling to geometrically increase both those messages and the opportunities to gamble, without a reliable, comprehensive prior study of their societal impact, fairly can be called irresponsible. Indeed, as a nation, we require an environmental impact statement for far less sweeping changes.

I am not advocating an impact study, however, for to me the reasonably-likely unhealthy impact of legalizing Internet gambling is clear, based on what I have witnessed in multiple cases and on over a decade of study. Moreover, to the extent that committee members or Congress might try, experimentally, to limit eventual legalization, regulation, and taxing of online gambling to, say, poker and non-sports gambling, and claim that these are different from and less problematic than electronic gambling machines, legislators will only be fooling themselves. Refinement of poker, blackjack, other card games, roulette, non-sports and sports gambling on computer terminals essentially has or will make these avenues of "entertainment" every bit as addictive, manipulative, and harmful as modern electronic slot machines.

You may be familiar with "When Pride Still Mattered," a fine biography by David Maraniss of the great N.F.L. coach Vince Lombardi. I focus here on the title of the book, hoping that, to this Committee, **pride still matters**. Indeed, the very opposite of pride would attach to any action by this Committee (or by Congress) which would encourage those gambling operators frothing at the mouth to gain increased and legitimized access to Americans' home and workplace computers, and thereby to Americans' savings, retirement funds, paychecks, grocery/utility/house payment/rent money, and to Americans' children, teenagers, pensioners, and the desperate. Advocates of legalized online gambling do not propose to build their businesses upon the occasional friendly bet. The industry runs on repeat business, aiming to extract the maximum "take" from bettors and replacing the tapped-out bettor with "new meat." The industry engages in sophisticated and expensive marketing efforts in support of these goals. The bill sets no loss limits or wagering standards; for example, it permits gamblers to play with illegal drug proceeds or to "lay-off" bets they take in operating their own illegal, unlicensed gambling enterprises. Non-gambling businesses, of course, also may engage in research-based and emotion-driven marketing and usually also seek to maximize profit, of course; but these non-gambling businesses usually produce a product or service having objective

value and do so without a business plan incorporating *sub rosa* deceit, predatory behavior, and criminality. The same cannot be said of Internet gambling operators.

As a nation, we have not even fairly tested the UIGEA and its too-long-delayed regulations. As a nation, we have not even attempted a sensible multi-specialty task force or coordinated approach to the problem of enforcement of laws existing before the enactment of the UIGEA. The *ad hoc* successes in a single federal judicial district (mine) of federal prosecutions like the BetonSports case and the Paradise Casino case and of federal forfeitures in the tens of millions of dollars from “vital service providers” to Internet gambling operations, strongly suggest that a coordinated, programmatic approach to the problem, especially now that the UIGEA tools are about to become more fully applicable, will succeed without disturbing anyone’s legitimate freedoms. If the Committee feels it must take some action, I would urge that it explore means of adequately-funding or demanding that the Department of Justice and/or the states’ Attorneys General establish such a task force, rather than continue the *ad hoc* approach of years gone by.

Local control over what vices will and will not be permitted in a community remains the essence of American government. Any federal legislation authorizing what will prove to be an unchecked spread and promotion of Internet gambling corrodes local values and undermines trust in national government. It will further diminish the evaporating reservoir of respect accorded elected officials. In a fundamental sense, your efforts as legislators are about whether, in a global economy, The People retain the authority in their communities to decide for themselves what activities and vices will be permitted. I urge you to not surrender that authority to the powerful syndicates and corporate interests presently spending millions on lobbyists seeking to delay implementation of UIGEA regulations, to repeal or gut the UIGEA, and with false and short-sighted appeals seeking legalization of Internet gambling in the U.S., whatever the costs. No tax you can pass will offset those costs.

I appreciate your consideration of my testimony.

“Biographic Blurb” attached to July 21, 2010,
Written Testimony of Michael K. Fagan

Michael Fagan served as an Assistant U.S. Attorney (AUSA) for the Eastern District of Missouri for twenty-five years, until February 2008, and now consults on domestic and transnational criminal law and procedure, anti-money laundering, counterterrorism, intelligence, and emergency planning issues. Selected as Coordinator of the Anti-Terrorism Advisory Council in 2001, Mike governed regional counterterror efforts in that role for over six years, and continues today as a Special Advisor to the Missouri Office of Homeland Security, as well as a member of the St. Louis Regional Response System Advisory Board.

The Department of Justice conferred on Mike the National Exceptional Service Award and the EOUSA Director's Award. Then-U.S. Attorney General Michael B. Mukasey recently noted Mike's "aggressive and creative prosecution of deserving defendants," citing as examples Mike's victories in the longest criminal trial in the history of the Eastern District of Missouri and crippling of the multi-billion dollar illegal offshore Internet gambling industry. The Chief of the Defense Intelligence Agency's USTRANSCOM Forward Element observed that Mike's "understanding of complex terrorist threats is second to none," enabling him to "powerfully contribute to the nation's security...." The Chief of the Justice Department's Organized Crime and Racketeering Section stated "Mike has single-handedly dealt a major blow to the illegal business of Internet gambling, making a difference in the lives of United States citizens throughout the country." The Director of the Executive Office for United States Attorneys praised Mike's "tenacity and creativity in identifying and developing new cases of an increasingly complex nature...." Former federal judge and CIA and FBI Director William Webster remarked that a May 2008 terrorism intelligence presentation by Mike at a conference held at Washington University in St. Louis was "the best of its kind that [Judge Webster] had ever seen." In addition to decades of gaining convictions in highly-sensitive and complex cases, Mike was the architect of proceedings resulting in approximately \$150 million in forfeiture and tax judgments in favor of the United States.

During his twenty-five year tenure as an AUSA, Mike served as a Special Attorney to the United States Attorney General from 1995 to 1997. He also served for three years as the Regional Coordinator for the Organized Crime Drug Enforcement Task Force. Mike taught at the National Advocacy College, as well as lectured at international, law school, corporate, law enforcement, and college training sessions. Prior to joining the Department of Justice in 1983, he spent a year as a litigator at Bryan, Cave, McPheeters, and McRoberts (now Bryan Cave LLC), in St. Louis. Mike began his law career as an Assistant Circuit Attorney for the City of St. Louis, after graduating from Washington University School of Law in 1977. He played college football at Southern Illinois University at Carbondale, from which he graduated with honors in 1974.