

Op-Ed/Editorials: Gambling and the Law®: Foreign Operators Don't Have To Pay U.S. Wagering Taxes

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A federal magistrate has just ruled that foreign internet gambling companies are not required to pay U.S. excise taxes on wagers, if the companies have been set up correctly. The decision is by no means final. But if upheld, it will eventually save internet operators billions of dollars, for bets taken from Americans.

Not that any of those companies are actually sending checks to the IRS. But their executives who made the mistake, say, of changing planes in Dallas, have been arrested and charged with tax evasion. A conviction means years in prison, and millions owed to the IRS.

The ruling was for one of the many pre-trial motions filed by Gary Kaplan, arrested in the Dominican Republic after his partner, David Carruthers, was caught in Dallas flying from his home in England to his business in Costa Rica. Kaplan, a former illegal bookie, had grown BetonSports into a billion dollar internet gaming company.

On April 28, 2008, Kaplan's lawyers convinced U.S. Magistrate Judge Mary Ann L. Medler that Counts 14 to 22 of the federal criminal complaint against him should be dismissed. These all claim that Kaplan attempted to evade the federal excise tax on wagers and "corruptly interfered with the administration of the revenue laws."

The Internal Revenue Code imposes an excise tax, much like a sales tax, on many wagers. Illegal bookies have to pay two percent of all bets they take. Many illegal bookies have contacted me for legal advice over the years. All of them tell me they pay this tax.

The modern casino sports book in Nevada was created when the excise tax on wagers authorized by state law was reduced to only one-quarter of one percent.

Kaplan admits that the sports bets he took were not authorized by state law. There seems little dispute that the BetonSports group booked \$3.5 billion in bets from 2001-2004. So, the Department of Justice says Kaplan owes \$70 million, before penalties and interest. And willfully evading this tax would mean years in prison.

But Kaplan has very good lawyers. And the first thing a good lawyer does is see what the law actually says.

It turns out this American excise tax does not cover bets made with foreign operators:

“The tax ... shall apply only to wagers

(1) accepted in the United States, or

(2) placed by a person who is in the United States

(A) with a person who is a citizen or resident of the United States, or

(B) in a wagering pool or lottery conducted by a person who is a citizen of the United States.”

This is what is known as a jurisdictional limitation. Congress does not have the power to tax all wagers everywhere in the world. It felt, correctly, that it could only tax bets made from the U.S. But it went even further.

Clearly bets accepted in the U.S. can be taxed. But what about wagers placed by Americans and accepted by foreign gambling operations.

There may have been no internet when this law was passed in the 1950s, but there were telephones. Congress expressly limited the 2% tax on cross-border wagers to overseas bookies who are American.

U.S. lawmakers probably did not want to start a tax war with other nations. A U.S. tax on Americans making bets with foreign licensed bookmakers would be like a tariff, More importantly, can the federal government tax a licensed foreign operators who never leaves his home country?

The DOJ argued that Kaplan, an American, owned BetonSports. But the magistrate held this was a real foreign corporation, not a mere sham.

This does not mean that Kaplan is out of trouble.

But it does mean that internet operators may have one less law to worry about, if they get good legal advice.

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