Routledge International Handbook of Internet Gambling

Edited by
Robert J. Williams, Robert T. Wood and Jonathan Parke
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5 Regulation and reputation
The Gibraltar approach

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Introduction
The rise of Internet gambling transformed not only the traditional ways of providing gambling, but also the established approaches to gambling regulation. With the prohibition of Internet gambling in the USA in 2006, the major Internet gambling operators concentrated their businesses on Europe. However, the competition from private Internet operators was being resisted by the majority of European Union (EU) member states. Despite numerous decisions by the European Court of Justice (ECJ), which appeared to support Treaty provisions for the free movement of services, the 2004 proposal of the Commission to include gambling into the Services Directive\(^1\) and a number of the infringement procedures,\(^2\) the national monopolies and protected markets continued to maintain and defend their position.

Risks associated with the industry, such as problem gambling or money laundering, have been used as the main argument for constraining the market. With the transformation of gambling into a transnational activity the nature of risks associated with this industry has also transformed: gambling risks have also become transnationalized. Therefore, in order to challenge existing rules and regulations, the Internet gambling industry must demonstrate its ability to manage the risks associated with its services. Risk management, however, does not pertain only to the risk of excessive gambling and crime. A significant feature of the risk relates also to organizational legitimacy. Contesting the perception of the public and policy makers by devising self-regulatory standards or managing ‘reputational risk’ (Power, 2007), is one of the strategies of Internet gambling operators to legitimize the industry. As argued by Levi-Faur (2005) efficient markets do not exist outside the state and the society in which they operate, and they require efficient regulatory frameworks which not only facilitate transactions and enhance trust, but also ‘mitigate negative externalities’ through the regulation of risk (p. 14). The few European jurisdictions that have decided to license and regulate Internet gambling, therefore, play a vital role in this process, with Gibraltar being one of the key players.

There are a number of reasons for choosing Gibraltar as a case study. First, alongside the United Kingdom and Malta, it was one of the first three territories within the EU to facilitate the establishment and development of Internet gambling by allowing private providers to operate from their territories and supply Internet gambling beyond those territories. It is also the EU territory with the longest relationship with the Internet gambling industry. Gibraltar argues to be the ‘unique’ Internet gambling jurisdiction: only licensing operators with a proven track record, requiring high technical standards as part of the licensing process, and with a commitment of management, staff, and IT infrastructure within the jurisdiction. The operators licensed in Gibraltar are undoubtedly the market leaders in terms of scale of online operations, and 7 out of 20 of them are publicly listed companies.
This chapter examines the ways in which Gibraltar regulates this newly emerging industry. It offers insights into the development of Internet gambling services in Gibraltar, the stability which is dependent on the reputation of the territory and the industry. The transnationalization of gambling, as well as the significance of the reputation and trust for both the industry and the territory require a combination of both private and state regulatory efforts. We therefore concentrate on the ways in which the Internet operators based in Gibraltar and the state actors ‘co-create’ the new regulations. It is argued that by legalizing and regulating Internet gambling, Gibraltar encourages the technological and the regulatory innovations necessary for the operation of Internet gambling. We address in particular the paradox between on the one hand the legitimization of the Internet gambling industry, and on the other the production of transnational risks, and on the other hand the development of sound Internet gambling regulation in order to reduce these risks. Whilst the state together with the industry becomes a risk producer, it is at the same time a risk taker and risk regulator.

In the next section we make the theoretical connection between offshore gambling and risk regulation, in particular the notions of ‘transnational risk’ (Beck, 1999) and reputational risk (Power, 2007). Subsequently the development of Gibraltar into an ‘Internet gambling hub’ will be outlined. This is followed by an analysis of the public-private ‘co-creation’ of regulatory standards for Internet gambling in Gibraltar. We conclude with an analysis of Gibraltar’s role in the shaping of EU gambling regulation.

Internet gambling and risk regulation

Thus far, scientific and political debates regarding the regulation of Internet gambling have focused primarily on the responses of the European institutions and the member states to the cross-border reach of Internet gambling, as well as the litigation and lobbying to which Internet gambling companies resort in order to promote their interests (Kingma, 2008; Della Sala, 2010). Such views, however, overlook the role played by the jurisdictions that accommodate, license, and regulate Internet gambling companies. The widespread common understanding of the phenomenon of Internet gambling, and its regulation and control, is in line with what Reed (2004) calls ‘The Cyberspace fallacy’:

The Cyberspace fallacy states that the Internet is a new jurisdiction, in which none of the existing rules and regulations apply. This jurisdiction has no physical existence: it is a virtual space which expands and contracts as the different networks and computers, which collectively make up Internet, connect to and disconnect from each other…. The world-wide accessibility of the Internet means that no one legal jurisdiction has de jure or de facto control of these activities. From all this, it is concluded that no jurisdiction has any control. (p. 1)

However, as several authors have argued, there is a real and material side of the virtual world of the Internet which is of crucial importance for understanding the phenomenon of the Internet itself (Castells 2001; Woolgar, 2002; Shields, 2003). While Internet gambling organizations may have a global reach, and may be flexible, networked, and virtual, they nevertheless always have a material existence somewhere, and are linked in many ways to local services, communities, and regulations. In order to avoid the cyberspace fallacy mentioned by Reed (2004), we will draw attention to the regulatory frameworks of the jurisdictions in which Internet gambling companies are located or have their licences.
Since 1994 when Antigua and Barbuda issued the first licence for an offshore remote gambling company, small offshore states have played an important role in the development of the industry. Not only do they accommodate the Internet gambling operators, they also challenge the existing onshore rules and legislations either themselves or via the industry. After the USA outlawed Internet gambling in 2006, Antigua formally challenged the ban via the World Trade Organization (WTO).

Although the origins of contemporary offshore economics have been linked with the creation of offshore financial centres, the developments of the Internet and telecommunications contributed greatly to the development of new offshore sectors such as Internet sex or Internet gambling (Palan, 2003). Prevented from establishing their businesses in onshore territories due to high tax rates or the absence or restrictions of legislative provisions and licensing systems, with few exceptions, gambling companies based themselves offshore to provide their services over the Internet. As argued by Palan (1998), the development of the offshore economy is promoting the development of juridical spaces ‘in which economic activities can develop more or less without hindrance’ (p. 64). By offering ‘residence’ via a licence acquisition many offshore tax havens, such as the Netherlands Antilles (Curaçao), Antigua and Barbuda, and Costa Rica, attracted hundreds of Internet gambling companies to their territories, offering a material basis for the advancement of the industry.

The expansion of the offshore economy and fierce competition between jurisdictions led, however, towards a ‘race to the bottom’ or regulatory laxity, which began in the 1980s (Palan, 2003). This contributed to growing concerns over the illicit nature of some offshore businesses, and major institutional bodies such as the Organisation for Economic Co-operation and Development (OECD), the International Monetary Fund (IMF), and the EU have expressed their concerns over the growth and nature of many offshore centres and transactions (Cobb, 2001; Palan, Murphy, and Chavagneux, 2010). Criticism from those institutions and the ‘onshore’ world resulted in the restructuring of many offshore economies. Offshore places began to reshape and promote themselves as reputable jurisdictions, which regulate, control, and supervise their services and products (Cobb, 2001).

We refer in particular to Hudson (1998) who provides strong arguments for understanding the origins and the development of offshore financial centres and their regulatory standards. By using the concept of ‘place’ developed by Massey (1993), Hudson argues that offshore centres are socially constructed places shaped by local and extra-local actors who are involved in regulatory bargaining, which is a process in which affected stakeholders negotiate and collaborate with governments in order to develop policies and regulations. Therefore, in order to understand the construction of offshore centres we must examine the positions of the governments and corporations and ‘the ways they relate to each other in the process of regulatory bargaining’ (Hudson, 1998: 918). Furthermore, trust is argued to be central to the social construction of places: ‘[S]ocial construction generates agreement on what place is’ (ibid.: 917); such agreement, however, depends on and reproduces trust. We suggest that trust relates to the idea of reputational risk discussed by Power (2007). We argue that reputational risk and reputation management are crucial for understanding the development of Gibraltar into the leading Internet gambling jurisdiction.

It has previously been argued that together with the legalization and liberalization of gambling markets, in which gambling becomes normalized as a consumer good, the regulatory focus shifts from a rule-based mode towards a risk-based mode of regulation (Kingma, 2004; Cosgrave, 2006). In the risk-based mode regulation focuses on the side effects and unintended consequences of commercial gambling, rather than on constraining the settings for gambling consumption and prescriptions for the operation of gambling
services. In the field of gambling, a rule-based approach might refer to a monopoly situation in which the operator is severely constrained; a risk-based mode might refer to exploitation based on free market forces which are only tempered in view of the risks relating to problem gambling and crime. An increasing awareness of, and regulatory focus on, side effects such as problem gambling and crime renders gambling part of the 'risk society' as defined by Beck (1992). Since Internet gambling may be characterized by the reduction of immediate controls and material constraints on the consumption of gambling services, the regulatory significance of gambling risks only increases.

To a certain extent the risk society already implies a 'world risk society' (Beck, 1999). With the transnationalization of gambling and the export of gambling risks to consumers based in jurisdictions other than those from which the gambling services are offered, the need for new modes of gambling regulation increases. The emergence of new issues triggers the emergence of new governance spaces with new networks of actors mobilizing to be involved and gain control, often challenging and undermining existing regimes and state control (Djelic and Sahlin-Andersson, 2006). Multiple actors such as non-governmental organizations (NGOs), civil society groups, or professional associations are increasingly involved in framing, shaping, and producing new rules and regulations in areas as diverse as finance, pollution, and education (ibid.). Furthermore, as argued by Power (2007), stimulated by scandals and catastrophic events, 'governance is being reinvented in terms of capabilities for effective risk management' (p. viii). Risk management has become central to the new kind of regulation, where correction of externalities becomes an integral part of modern regulation.

Both the state actors and the industry are acting in an environment of uncertainty, where failure is possible and the legitimacy and reputation of the participants are at stake. Modern states have recently become explicit about risk management and are increasingly adopting concepts and standards from the private sector (Power, 2004). By adopting risk-management practices the state attempts to improve its ability to control risks. States are increasingly preoccupied not only with the minimization of negative externalities through regulation, but also with the management of public expectations and perceptions towards the state's ability to manage risk.

To minimize the undesirable side effects of activities and manage risks posed to the reputation of the state, regulatory agencies are created, which in turn employ risk-based 'responsive' approaches to regulation (Power, 2004). In the risk regime of regulation, self-regulation at the organizational level of gambling operators is as important as state regulation (Kingma, 2004). According to Power (2007), the rising significance of risk management represents a new phase of corporate governance. In this new phase internal control becomes as important, and sometimes takes precedence over, external control and regulations. Self-regulation and compliance to normative rules of organizational conduct become the new standard to which external control agencies develop a complementary role. The work of external control agencies, which becomes relevant in case of failure of internal controls, is defined in terms of meta-control or 'the control of control'.

An approach which is described as 'enforced self-regulation', which combines state and corporate regulatory efforts (Hutter, 2006), often relies on the internal controls and self-organization of regulatees. Accordingly, private sectors and professional services are becoming co-creators of risk management and regulation. The government broadly outlines standards which the private sector is expected to meet. The private sector develops risk-management systems and rules to secure and monitor compliance, as well as the procedures that deal with non-compliance. The role of the regulatory officials is to oversee this process. The expertise of private actors in technically complex areas is one of the reasons why
regulators increasingly rely on private actors to shape policy (Heritier and Eckert, 2008). Risk-based regulation can be used as a part of the regulators' own reputation risk-management process (Power, 2004). Therefore, at the local level state and private actor networks work together to create a place-specific regulatory model which is ultimately affecting the perception of a jurisdiction as a safe and reputable place to operate from, and contributes to an increase in the client network via direct and indirect marketing strategies (Cobb, 2001).

With regard to reputational risk management, it is important to emphasize that the reputation of the offshore centre, Gibraltar, and the Internet gambling industry are intertwined: Gibraltar needs to be perceived as a reputable jurisdiction to ensure economic stability of the territory, which is partially reliant on the Internet gambling industry. Therefore Gibraltar must find a regulatory balance between controlling the industry and allowing for its development. The Internet gambling sector is counting on the reputational advantages of being licensed and regulated in a reputable jurisdiction with a tight regulatory regime in order to legitimize itself. Moreover, being licensed by an EU member state empowers the Gibraltar industry to challenge existing regimes and pursue their interests on the European level in order to gain access to the European-wide market. Regulation of the industry by Gibraltar not only enhances legitimacy and trust, but also has political implications. It has enabled the argument for Treaty enforcement with regard to the free movement of services, promoted the current revision of gambling legislation in a number of the EU member states, stimulated action towards the development of an EU Directive by the European Commission, and provided a 'collaboration' agenda for subsets of each six-month Presidency for a number of years.

**Gibraltar as an Internet gambling hub**

When in 2000 the OECD identified Gibraltar as one of the 35 jurisdictions that met the technical criteria for being a tax haven, the government of Gibraltar decided to re-adapt their strategy for economic development. The government made a commitment to improve the transparency of its tax and regulatory systems. The steps taken by Gibraltar have included the abolition of the tax-exempt company scheme, the signing of 18 Tax Information Exchange Agreements, and tax system reform which reduced company tax from 22 to 10 percent for all companies, and therefore ended the distinction between onshore and offshore business.

The perception and reputation of Gibraltar is, therefore, of paramount importance to the Gibraltar government. The Chief Minister commented in an interview: 'our international reputation is about the only economic resource that we have at the core of all our economic policies.' This concern not only relates to Internet gambling but builds upon policies that were developed for the regulation and overhaul of the finance and shipping sectors. The concern over reputation was partly developed in response to outside pressures from international organizations such as the OECD. At the same time the influence of the local authorities should not be underestimated. In 1996 the Chief Minister Peter Caruana and his administration committed to the transformation of Gibraltar's reputation and its economy. Their efforts have been acknowledged by much of the local population, international organizations, and the businesses based in Gibraltar. A Gibraltar lawyer commented on this fact as follows:

It could be argued that the last [2007] elections the Chief Minister has won because of how well he has done with this [Internet gambling] and the other. Bringing the reputation of Gibraltar to a high standard, 12, 14 years ago Gibraltar was not considered a reputable jurisdiction. Now it is, widely it is.
Also, the businesses based in Gibraltar, including Internet gambling companies, are not relocating from the territory despite the fact that from 2011 the tax rate is significantly higher after tax reform. Having paid 1 percent gambling duty with a ceiling of €500,000 per year, from 2011, Internet gambling providers will be exposed to 10 percent company tax. Their decision to stay in Gibraltar underlines the importance of the territory’s reputation as the leading Internet gambling jurisdiction and the robustness of its regulatory system, as well as the relations between the local authorities and the industry.

The development of Gibraltar into an Internet gambling hub took place in three phases. The foundations of Gibraltar’s Internet gambling industry were established as early as 1989, when Gibraltar issued its first ‘offshore gambling licence’ to a local bookmaker to cater for betting by non-resident customers. After the reopening of the Spain-Gibraltar border in 1985, British nationals residing in Spain could finally visit Gibraltar and Gibraltar’s betting shops. High street betting shops so popular in Britain were not present in Spain, so the reopening of the border enabled them to bet again. However, the Gibraltar betting entrepreneur had to compete with the well-known and established British bookmakers, who were also taking bets over the phone. The offshore gambling licence which allowed the taking of bets from customers residing outside of Gibraltar with only 1 percent betting tax gave a competitive advantage at a time when betting with the UK-based operators meant paying 9 percent tax.

The second phase started in 1993 when the British betting company Ladbrokes opened their telephone betting operation in Gibraltar. In this phase the development of higher volume offshore betting began, providing the local government with considerable income and a boost for employment in the territory through betting management and call centres. In 1996 Victor Chandler International, another British bookmaker, was also granted a Gibraltar betting licence. Until 1999 the impact upon the United Kingdom betting market was constrained by a voluntary code between the offshore-based operators which agreed not to accept bets from British customers (HM Treasury, 1999). The code was breached by Victor Chandler International in May 1999, which started actively servicing UK customers. The violation was triggered by the decision of the Irish government to cut betting tax from nearly 10 to 5 percent. This was seen as a huge threat to Victor Chandler International, which feared losing UK clients to Irish betting operators (Doward, 2000). Other bookmakers followed the lead of Victor Chandler International. Initially servicing customers mostly from the Far East, in 1999 Ladbrokes started offering betting services to British customers over the phone or fax without 9 percent betting duty; it was employing 250 people in Gibraltar. An attractive tax regime, and the same currency and language appealed to other well-known bookmaking companies and other British operators such as Stan James also gained a licence and moved their operations to Gibraltar, creating over 500 jobs. Typically, the bookmakers offered nil deductions over the Internet and only 3 percent over the telephone (HM Treasury, 2000).

The actions of Gibraltar and of the bookmakers, causing an exodus of the major British bookmakers to Gibraltar, was met with criticism by the British Treasury which accused the bookmakers of exploiting a loophole in the advertising ban by promoting ‘tax-free’ offshore betting in the United Kingdom using teletext services (HM Treasury, 1999). By that time the benefits of the betting industry were recognized by Gibraltar, and Gibraltar authorities were eager to guard their ‘right to have their own taxation and powers’ (Panorama, 1999). Gibraltar obtained this right in 1969 with the formation of the Gibraltar House of Assembly and the 1969 Constitution (Garcia, 2002). But the Gibraltar government was cautious about the industry’s growth and the potential damage which the gambling industry could cause to the image and reputation of the jurisdiction. For this reason, Gibraltar capped the number of licences to seven, making Gibraltar licences the most desirable ones. The last, seventh
licence, was obtained by Simon Bold, the founder and main shareholder of Liverpool-based Mawdsley Bookmakers. In 1999 Simon Bold moved to Gibraltar founding Simon Bold (Gibraltar) Ltd, operating telephone and Internet betting. Simon Bold was subsequently acquired in 2001 by betandwin.com for the price of around £2 million in shares and cash (Klein, 2001). The acquisition of Simon Bold and the Gibraltar licence was seen by the Austrian betting company bwin as a gateway to international markets. It was the first Gibraltar licence not to be obtained by a well-known British bookmaker, which was diversifying its own means of offering betting to include phone and Internet.

Bwin was established in 1997 in Austria as an Internet bookmaker without prior experience in operating betting shops. The company grew rapidly and within three years, bwin completed the most successful initial public offering in the history of the Austrian Stock Exchange, raising capital of €55 million (www.bwin.ag).

In 2001 the British government removed betting duty and replaced it with a lower-cost ‘Gross Profits Tax’ in order to ‘stop the boom in offshore tax-free gambling which costs the exchequer millions of pounds a year’, thus making Gibraltar betting licences less attractive (BBC News, 2001). Some British operators moved their telephone betting services back to the UK. For example, Ladbrokes took this step, reducing their Gibraltar workforce from 250 to 25 in late 2001.6

During this time the third phase took shape. In this phase the dot com boom took Internet gambling to a new level. The industry diversified and as well as telephone and Internet sports betting, it had started offering Internet poker, casino games, bingo, lottery, and betting exchanges, turning over hundreds of millions of dollars per year. Moreover, the long-lasting disputes over the legality of Internet gambling supported by the 1961 Wire Act7 in the USA, and the subsequent passing of the Unlawful Internet Gambling Enforcement Act ( UIGEA) in 2006, contributed to the suspension of real-money operations by many Internet gambling providers. All Gibraltar operators suspended their services in the USA. This meant that the European market became the main market for Internet gambling. Being located in a European jurisdiction was vital if the operators wanted to argue for EU-wide regulation. As the co-CEO of bwin explained during an interview:

In 1999 there were few places that you could go to – Gibraltar, Isle of Man and the Caribbean. We thought, well, if we do it, we have to stay in Europe. We cannot argue a European case being in Antigua, so we had to join either the Isle of Man or Gibraltar.8

The demand for the European licence grew and apart from the betting licence, in 1998 Gibraltar introduced a parallel casino licence which permitted a variety of gaming products to be provided through the Internet. Ladbrokes were among the first to set up their Internet casino gaming operation in Gibraltar. In this phase of development, in order to control the industry and minimize the reputational risk, the Gibraltar government continued its strategy of controlled growth for the gambling industry despite the absence of economic pressures from the UK government that had applied in respect of betting taxes. Standards initially set by the established British bookmakers had to be maintained and, as explained by the Chief Minister, Gibraltar was looking for:

partners in looking after the jurisdictional reputation and we were looking for companies that would attach as much importance to their corporate reputations as we did for our jurisdiction reputation. And because we felt that that would give us a sort of partnership of the willing and would make the regulatory system easier to deliver...9
A further reason for Gibraltar’s careful and restrictive approach to Internet gambling was the government’s desire to maintain the diversity of the Gibraltar economy. The Gibraltar government is not willing to rely on a single business sector for the stability of the economy. Although they actively limited the number of licences, nearly 10 percent of the Gibraltar workforce was employed by the gambling industry in 2010. The benefits from Internet gambling companies are not limited to gaming tax and employment opportunities, they also create upward demand on the Gibraltar telecommunication infrastructure, employees pay their income tax in Gibraltar, rent offices and accommodation, and create demand for legal, banking, and other services.

As underlined by the Chief Minister, due to the relatively small size of the Gibraltar economy, Gibraltar does not require a large number of gambling companies in order to have a significant impact on the local economy. By careful selection of their gambling operators, Gibraltar opted for quality rather than quantity, and brought together parties for the co-creation of a regulatory regime, comprising a small number of ‘reputational risk-sensitive’ operators, with a government prepared to allow them to operate within that risk framework.

Currently, as of March 2011, 20 operators are licensed in Gibraltar. They hold a total of 35 licences: 21 for gaming, 13 for betting, and one for spread betting in financial products. An overview of the companies present in Gibraltar in 2011 as well as their gambling activities is presented in Table 5.1.

The Gibraltar Internet gambling operators are represented by the Gibraltar Betting and Gaming Association (GBGA), which was formed in 2003. All operators licensed in Gibraltar are members of this association. The chairman of the association is the Gibraltar bookmaker who was granted the first offshore betting licence in Gibraltar. He currently works for PartyGaming. The GBGA acts as an interlocutor between the industry and the government, which work together not only on regulatory issues, but also on solving local problems that the industry encounters, such as infrastructure development, the price and reliability of telecommunications, and the labour market. Apart from everyday issues the industry also works closely together on maintaining the good name of the operators and the jurisdiction.

In the case of Gibraltar, ‘cooperation’ also means physical proximity. The scarcity of space has always been a defining condition for any organizational practice in Gibraltar. This scarcity not only implies business constraints but also serves as an enabling condition because close proximity means more opportunities for synergy between businesses and face-to-face cooperation. Up until the 1990s, when the military presence was starting to diminish, only 20 percent of the territory was accessible to civilians. New office and housing space had to be found promptly in order to accommodate the demand from the services sector. Land reclamation allowed for some expansion of the territory and multiple modern office and housing estates have been constructed within a decade. The Europort building complex, which was built in the early 1990s, has accommodated eight Internet gambling companies and their 400 employees as well as the gambling regulator. Literally across the road in the Eurowellers, two more gambling companies have their offices and a few cafes and restaurants where employees go for their morning coffee, lunch, or dinner. Within a 10-minute walk you can reach Watergardens, another modern complex, where a further four gambling companies are situated. The rest are scattered around the town, but all of them are within walking distance of each other and the regulator. Such proximity and the unavoidable informal contacts it creates between management, staff, technicians, regulator, and the wider public should not be underestimated in terms of enhanced communication links and quality and speed of information sharing.
<table>
<thead>
<tr>
<th>License operators</th>
<th>Gambling activity</th>
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</thead>
<tbody>
<tr>
<td>Ladbrokes (International) Ltd</td>
<td>Betting</td>
</tr>
<tr>
<td>Ladbrokes Sportsbook LP</td>
<td>Gaming</td>
</tr>
<tr>
<td>Victor Chandler (International) Ltd</td>
<td>Betting</td>
</tr>
<tr>
<td>Eurobet (Gibraltar) Ltd</td>
<td>Gaming</td>
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<tr>
<td>Stan James (Gibraltar) Ltd</td>
<td>Gaming</td>
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<tr>
<td>Bwin International Ltd</td>
<td>Gaming</td>
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<tr>
<td>(Ongame Network Ltd)</td>
<td>Gaming</td>
</tr>
<tr>
<td>Tower Rock Limited (Carmen Media Group Ltd)</td>
<td>Gaming</td>
</tr>
<tr>
<td>St Minver Ltd</td>
<td>Gaming</td>
</tr>
<tr>
<td>32 Red Plc</td>
<td>Gaming</td>
</tr>
<tr>
<td>Digibet Ltd</td>
<td>Betting</td>
</tr>
<tr>
<td>Cassava Enterprises (Gibraltar) Ltd (888.com Plc)</td>
<td>Gaming</td>
</tr>
<tr>
<td>11 Mansion (Gibraltar) Ltd</td>
<td>Gaming</td>
</tr>
<tr>
<td>12 Partygaming Plc (PGB Ltd) (ElectraWorks Ltd)</td>
<td>Gambling</td>
</tr>
<tr>
<td>13 Prospects Limited (formerly FuturesBetting.com Ltd)</td>
<td>Financial spread betting</td>
</tr>
<tr>
<td>14 Partouche Interactive (Gibraltar) Ltd</td>
<td>Gaming</td>
</tr>
<tr>
<td>15 WHG (International) Ltd (formerly William Hill (Gibraltar) Ltd)</td>
<td>Gaming</td>
</tr>
<tr>
<td>WHG (International) Ltd</td>
<td>Betting</td>
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<tr>
<td>WHG Trading Limited</td>
<td>Gaming</td>
</tr>
<tr>
<td>WHG Trading Limited</td>
<td>Betting</td>
</tr>
<tr>
<td>16 Hillside (Gibraltar) Ltd (Bet365 Group Ltd)</td>
<td>Gaming</td>
</tr>
<tr>
<td>17 Pelfre (Gibraltar) Ltd (Betfred)</td>
<td>Betting</td>
</tr>
<tr>
<td>18 Gamesys (Gibraltar) Ltd (formerly Entertaining Play Limited)</td>
<td>Gaming</td>
</tr>
<tr>
<td>19 Probability (Gibraltar) Ltd</td>
<td>Gaming</td>
</tr>
<tr>
<td>20 Betfair</td>
<td>Betting exchange</td>
</tr>
</tbody>
</table>

Source: Adapted from Government of Gibraltar, Information Services (www.gibraltar.gov.gi) and GRA (2009/10).
The Gibraltar regulation approach

Gambling regulation in Gibraltar builds on the general approach to regulation which Gibraltar has adopted during recent years. The initial decision to license a small number of well-known and established risk-sensitive operators could be seen as a way of safeguarding the reputation of the territory. Unlike other jurisdictions that are interested in attracting as much business as possible to their territories, Gibraltar has not accepted ‘brass plate’ licensing of Internet gambling companies. Brass plating permits gaming servers to be located within the territory but management and control to rest elsewhere in the world. As such, they are beyond the statutory powers of the licensing government and regulator, which instead rely on an agreement to accept ‘extra-territorial’ supervision by the travelling regulator and return to the licensing jurisdiction on an occasional basis. Paradoxically, it is not uncommon for brass plate licence holders to be unlicensed in the state where their management and control are exercised, with a head office and company direction and supporting activities acted out without direct regulatory constraints but notionally to the written rules of the licensing jurisdiction. This dissociation of management control from technical operations has more in common with the early uncontrolled offshore enterprises and is largely compensated for by rule-based regulation as opposed to the risk-based approach, with the out-of-state parties provided with and required to demonstrate detailed application of systems and procedures.

Gibraltar’s public position is that of ‘home to the world’s leading online gambling operators’ (GRA, 2009/10), and ‘something of an online gambling capital’ (Atkinson, 2006). However, Gibraltar does not actively seek to attract Internet gambling providers to the territory. On the contrary, on their website, the Gibraltar government openly ‘warns’ the potential applicants that ‘Licences are generally difficult to obtain’.

In order to maintain the position of a reputable jurisdiction, which remains vulnerable to process failures due to error, slippage in standards, or simply being overtaken by new malicious attacks, the Internet gambling industry is supervised and controlled by the government. As previously touched on, this control starts with a strict licensing process that does not accept applications until the interested party is able to satisfy the government of its reputational foundations. A solid background and an unquestionable business plan constitute the first of the requirements. Also, the operators must meet the government policy of developing and maintaining a substantial presence in Gibraltar. Companies must maintain legal and physical offices in Gibraltar, establish management positions and a number of employees (Gibraltar Licensing Authority, 2011). The diversity of the operators’ antecedents and operating structures means that some of the companies maintain their headquarters and support centres in other jurisdictions with equivalent or proportionate regulatory or corporate governance regimes. They are allowed to operate from Gibraltar on the basis that they locate key management and operational personnel and equipment there. Other companies have their headquarters based in Gibraltar, but support, or non-licensable functions elsewhere. This is a reflection of the globalization of the product and the markets, with low-cost states providing low-risk activities (call centres, IT development) and higher-risk, licence-triggering, or control activities at the centre.

Another important aspect of the licensing process is due diligence, in particular the checks on key personnel and technology. For all the managerial positions in Gibraltar a series of checks are conducted in order to establish whether people behind the operation are ‘fit and proper’. Background probity checks, as well as establishing whether they have sufficient knowledge and experience to hold and properly conduct respective positions is coupled with detailed financial and criminal checks. Gibraltar law enforcement agencies work together
with financial intelligence agencies that provide them with information on criminal records and international intelligence reports. Any changes in key personnel must be submitted for approval.

The technology that underpins the operation must also be approved in terms of its architecture, location, and content. This task is shared between independent test houses, which have also been approved for competence and checked for integrity, and the regulator or his authorized nominees. Five test houses\(^\text{12}\) based in the UK, Australia, and Canada have thus far been approved for this purpose. The role of test houses is to analyse software and equipment against manufacturers’ specifications and legislative and regulatory requirements.\(^\text{13}\) All operators must be able to demonstrate that their games and systems meet relevant standards within a dynamic, complex, and highly competitive industry.

The introduction of the new Gibraltar Gambling Act in 2005 could be considered as the consolidation of Gibraltar’s regulatory approach to Internet gambling. The 2005 Gambling Act came into operation in October 2006, repealing the 1958 Gaming Act. It avoided detailed prescription and sought instead to provide a new regulatory framework for Gibraltar’s gambling industry. For the first time a specific provision was made for Internet gambling, covering the principles of technical and professional competence, player protection, and the integrity of gambling products. The purpose of the Act was to ‘modernise Gibraltar’s legislation and to create a statutory licensing and regulatory framework to suit Gibraltar’s status as “home to the world’s leading online gambling operators”’ (GRA 2009/10: 71).

The Act also created a new body, the Gambling Commissioner, with supervisory responsibilities then being divided between the Licensing Authority and the Commissioner. The Licensing Authority is designated as the Minister responsible for gambling. At present the Chief Minister, who is also the Finance Minister, carries out this function. Unusually, the government takes direct responsibility for its policy decisions. The Licensing Authority carries out its functions through the Gambling Division of the Ministry of Finance, and is responsible for evaluating applications, determining and amending licences, and imposing terms and conditions on licencees.\(^\text{14}\) The direct and close involvement of the head of government demonstrates that Internet gambling is regarded as a key industry in Gibraltar.

The Gambling Commissioner, which is currently designated to the Gibraltar Regulatory Authority (GRA), is responsible for ensuring that the holders of licences conduct their undertakings in accordance with the terms of their licences and provisions made by the Act (ibid.). Amongst the legislative provisions is that they should do so ‘in such a manner as to maintain the good reputation of Gibraltar’ (Government of Gibraltar, 2005). We observe here, that in Gibraltar the concern for reputation is instituted by law.

The Gibraltar Gambling Act introduces a minimum age for participation in gambling. It also makes specific provisions for responsible gambling and for money laundering. Although the Act broadly indicates the requirements relating to, for instance, the minimum age for gambling, the specific methods to achieve those requirements are left to industry self-regulation, overseen by the Gambling Commissioner. The Act states: ‘A licence holder shall take all reasonable steps to prevent any person from participating in the gambling activities provided by the licence holder unless he is at least of the minimum permitted age’ (section 37, [1]). Moreover, the Act obliges Internet gambling operators to establish and maintain effective systems of internal controls and procedures in order to monitor their activities. This is a clear case of enforced self-regulation. It also indicates a reliance on the industry standards and procedures to achieve desired regulatory outcomes. Regulation must remain flexible in order to be able to provide for the constantly evolving industry and the methods and practices available to it to meet regulatory obligations. Therefore, broad guidelines are provided and
the industry is empowered to implement procedures which will enable them to satisfy those guidelines. Although further specifications and somewhat more detailed guidelines were introduced by the Code of Practice for the Gambling Industry in 2009, the regulator remains consistent in this broad approach to regulating the industry:

It is the Gambling Commissioner's preference to keep the scale of formal requirements to a necessary minimum, and deal with as much guidance as possible by way of the more flexible and speedy codes of practice, as opposed to seeking statutory Regulations.

(GRA, 2009)

In section 5.3 of the Generic Code of Practice, which develops the principles of the Gambling Act, the regulatory expectations on 'self-exclusion systems', which offer customers the option of excluding themselves from an operator's gambling services, the Code of Practice explicitly recognizes the self-regulatory standards devised by industry associations:

Subject to the Gambling Commissioner's further advice, self exclusion systems modeled on mainstream industry bodies' advice, and recognised by the Commissioner, such as GamCare, eCorga and RGA, will be regarded as effective systems for the purposes of this requirement.

In section 7.3, the Code of Practice further specifies the areas which the industry should include into their internal controls and operating procedures required by the Gambling Act. They include:

- corporate structure and reporting; internal and external audit arrangements; accounting and financial control standards; customer and transaction controls (including fraud and security arrangements); business continuity/disaster recovery plans; anti money laundering arrangements; age verification procedures; problem gambling and self exclusion policies; customer complaints arrangements; system testing and security arrangements; and web content and customer control measures to ensure that sites do not contain or access inappropriate material.

The aforementioned provisions clearly indicate that the Internet gambling industry is expected to effectively self-regulate and institute structures and procedures required by law, or run the risk of having less flexible and dynamic arrangements imposed on it.

Heavy reliance on the regulatory capacity of the regulatees, and their responses to the legal requirements constitute, however, one of the weaknesses of the enforced self-regulation approach (Hutter, 2001). The effectiveness of self-regulation ultimately depends on the 'control of control', i.e. the extent to which self-regulation is actually monitored and maintained.

In Gibraltar the regulator works in close cooperation and consultation with the Licensing Authority and the industry. The industry was consulted to provide their input with regard to the 2005 Gambling Act. The Code of Practice and the 2010 Anti Money Laundering Arrangements are also the result of public-private cooperation between the regulator and the industry. The industry is currently involved in developing the Remote Technical and Operating Standards. The industry is invited to respond to the proposed documents, but importantly, the regulator and the industry frequently meet face to face during the GBGA meetings and individual encounters. This process of consultation not only allows for the
content of the legislation to be established, but it is also a vital learning and knowledge-sharing experience. During the process both parties learn and discuss their respective priorities, expectations, and concerns. Exchanges take place at short notice and the regulator is able to meet personally with the key personnel of the companies and the employees. The physical proximity coupled with the requirement of physical presence of personnel in Gibraltar, therefore, contributes to the uniqueness of the territory and its gambling regulatory regime.

Regulatory engagement with operators is achieved through a range of more structured, but complementary processes. Customer complaint monitoring and investigation provide the most significant indications of non-compliance with the regulatory standards. The nature of customer complaints captures the diversity of the engaged population. While complaints may centre on the misunderstanding of rules, they extend to customers' discovery of second- and third-tier 'bugs' in software, i.e. a coding error that requires a prior or two prior events to occur before it can be triggered, or even 'non rational' events to be selected by the player to trigger the 'error'. Such is the focus of many players' attention to the performance of games, even for trivial sums, that coding errors are quickly identified and invariably exploited, with the deviation from truly random outcomes stimulating anomalous play and payout patterns.

Substantive complaints invariably involve an examination of the operator's adherence to compliance policies and the decision making of staff. They trigger visits to an operator's premises, examination of records, and direct explanations of events. Complainants may be quick to point out real and imagined compliance failures by operators to support their claims. Complaints can be managed promptly, as physical proximity and the number of operators allows the regulator to act without delay. The proximity as well as the requirement to maintain a substantial presence in Gibraltar again also allows the regulator to visit licensees and examine their equipment and operations to ensure compliance with Gibraltar's regulatory model.

The regulator also employs intelligence mechanisms to monitor the activities and conduct of the operators. This includes information from foreign authorities and regulators as well as checks performed via Internet search tools, gambling-related forums, and blogs. Reports and self-reports from the industry constitute another control mechanism employed by the regulator:

- Regulatory Returns Reports provide statistical information about the operators' activities. This includes information about responsible gambling, complaints, and operational data.
- Licence holders’ incident reports are also requested on an ad hoc basis with respect to specific compliance breaches and failures and the regulator expects the industry to report any substantive breach, threat, or contravention of Gibraltar’s regulatory model.

Moreover, in an industry where reputation holds so much importance, best practices executed by one operator are frequently observed and adopted by others, whereas bad practices and behaviour are often flagged by customers or competitors. The small location, employees changing companies, and friends and family members working for competitors, means that operators gain an insight into what their competitors are doing. The high value of Gibraltar's gambling licence for the industry means that the operators are willing to comply with conditions and rules imposed on them by Gibraltar's authorities. The co-creation of those rules also commits the industry to compliance.

The robust regulatory regime as well as monitoring mechanisms might be vital for the industry in its attempts to expand the European market, where Gibraltar as well as the Internet
and knowledge—their respective and the regulator employees. The personnel in enabling regulatory re-structured, but tion provide the ds. The nature of complaints may of second- and o prior events tol by the player to dance of games, y exploited, with payout patterns. or's adherence to an operator's claimants may be port their claims. ber of operators ment to maintain sit licensees and ullar's regulatory ities and conductulators as well as d blogs. Reports m employed by rators' activities. operational data. s with respect to industry to report y model.

actices executed ad practices and ition, employees ors, means that the of Gibraltar's to comply with creation of those be vital for the all as the Internet gambling industry has to 'convince' the public and policy makers that they are reliable, reputable, and heavily regulated. The Internet gambling industry has to demonstrate that it is committed to managing the transnational gambling risks such as underage gambling, problem gambling, money laundering, and match-fixing.

Conclusion

In this chapter we have analysed the development of Gibraltar into the world's primary Internet gambling jurisdiction. We argued that offshore jurisdictions play a crucial role in the development of Internet gambling, and that for Gibraltar reputation is a major asset and concern. Internet gambling companies perceive Gibraltar as a legal and reputational gateway to the EU market. There is growing evidence that the USA has the same perspective with a series of US/Gibraltar joint ventures reported in industry media and Gibraltar remaining unblemished by the 'Black Friday' indictments of April 2011. This has turned Gibraltar into a producer and manager of 'transnational' gambling risks related to underage gambling, problem gambling, and fraud. In order to address these risks and maintain a good reputation Gibraltar recognizes that a solid regulatory framework for the Internet gambling industry is a vital interest. In this conclusion we would like to draw attention to three major points.

First, for Internet gambling, a regulatory framework and a solid reputation are not self-evident features of offshore jurisdictions, but should rather be viewed as active policy achievements. In this respect the Gibraltar regulatory framework for Internet gambling is consistent with the regulatory approach developed for the financial sector. The Gibraltar authorities, however, did not want to make the economy over-reliant on a single sector. At the same time developments in global telecommunications provided new opportunities for the gambling industry to offer their services remotely and expand their markets. By offering competitive taxation levels and an adaptive regulatory regime Gibraltar attracted a number of British bookmakers to the territory wishing to take advantage of taxation and regulation differentials between Gibraltar and the UK.

Second, the settlement of Internet gambling companies and the application of gambling regulations did not immediately constitute Gibraltar as an Internet 'gambling hub' but rather meant the beginning of a transitional phase in which Gibraltar developed new regulatory standards and procedures under direct supervision of the Chief Minister. The development of the Internet gambling business and regulation involved a differentiated network of actors who gradually 'enrolled' in the policy-making and regulatory process, notably the Chief Minister, the GRA, the Gambling Commissioner, the Internet gambling companies, and the GBGA. In the process of public–private 'co-creation' of regulatory standards, gambling practices were modified and new regulatory standards emerged. This process included the development of specialized artifacts such as the 2005 Gambling Act, the Codes of Practice, and more mundane aspects such as the Europort complex which accommodates the regulator and many operators. The strategy of controlled growth was crucial because it made the licences a scarce and precious resource to the operators. We have drawn special attention to the role of reputation management which was explicitly referred to in the Gibraltar Gambling Act. Reputation should therefore not be regarded as a mere side effect of gambling operations but as an effect which, in terms of reputational risk (Power, 2007), now forms an integral part of the regulation of Internet gambling.

Third, the Gibraltar regulatory approach to gambling involved the introduction of a specific balance between state authorities and regulators on the one hand and Internet gambling organizations on the other. The Gibraltar approach is not only characterized by close
cooperation and the co-creation of regulatory standards, but also by the model of enforced self-regulation. This model means that governments establish broad standards and oversee the process of industry compliance with the standards. However, it is the companies themselves who further specify the rules and develop risk-management systems and systems of compliance and monitoring of that compliance. In this model regulation becomes dependent upon the commitments and capacity of the industry, and the ability of the state to find and maintain an optimal monitoring role. For the Internet gambling industry, being based and regulated in Gibraltar is vital to the pursuit of their argument for the open European market.

Notes
1 Directive 2006/123/EC on services in the internal market was designed in order to establish free market for services in the EU by simplifying national procedures and removing barriers to provision of cross-border services. It was adopted by the European Parliament and the Council on 12 December 2006.
2 EU member states are responsible for the implementation and compliance with EU law. If a member state fails to comply, the European Commission can open an infringement procedure against that state. Initially, the Commission itself attempts to bring the infringement to an end. However, if the member state does not conform voluntarily it may refer the case to the ECJ. Infringement procedure follows several formal stages.
3 An Exempt Company was a non-resident company that was exempt from corporation tax on the profits of the company and instead paid a fixed annual duty between £225 and £300 to the Gibraltar government.
4 Interview with Chief Minister Peter Caruana, October 2010.
5 Interview with Gibraltar lawyer, November 2008.
6 Interview with respondent 4.
7 The Wire Act prohibits interstate telephone betting but pre-dates the Internet and has not been amended to include it.
8 Interview with co-CEO of bwin, January 2009.
9 Interview with Chief Minister Peter Caruana, November 2010.
12 The test houses are: Technical Systems Testing (TST); eCommerce and Online Gaming Regulation and Assurance (eCOGRA); iTech Labs Australia (iTech); Gaming Associates Pty Ltd; Gaming Laboratories International Europe B.V.
13 www.gamingassociates.com
14 Email communication with N. Macias, Assistant Gambling Supervisor, December 2008.

References
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