

# ONLINE CASINOS FORCED TO FOLD: EXAMINING THE EFFECTS OF *IN RE BAUM*, 386 B.R. 649 (BANKR. N.D. OHIO 2008)

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## I. INTRODUCTION

In 2007, gross gambling revenue for all legalized gambling in the United States<sup>1</sup> totaled 92.27 billion dollars.<sup>2</sup> Online gambling, however, is not a part of this calculation because of recently passed legislation prohibiting the collection of debt that was issued for the purposes of online gambling, such as a credit card used to play poker at an internet casino.<sup>3</sup> This statute, the Unlawful Internet Gambling Enforcement Act of 2006 (UIGEA)<sup>4</sup>, was recently applied by *In re Baum*.<sup>5</sup>

In *Baum*, the court addressed the issue of enforceability of credit card debt as it applies to online gambling.<sup>6</sup> The case involves a woman who filed for bankruptcy after running up almost \$40,000 worth of credit card debt due to her excessive online gambling.<sup>7</sup> Applying the statute to the facts of the case, the court ruled that the credit card debt was void and could not be collected under federal law.<sup>8</sup>

*Baum* is important because it is the first case that applies this relatively new statute, and it illustrates the extreme burdens created by the law. First of all, the statute is difficult to apply due to definitional ambiguities. Furthermore, the regulations promulgated under the statute create an absurd situation whereby it is legal for American citizens to gamble online with a credit card, but illegal for financial institutions to allow such credit card transactions to occur. These regulations also do not apply to foreign entities, so American financial institutions bear the entire burden of this proposed resolution to the “problem” of internet gambling in

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1. This figure is calculated by the amount wagered minus the winnings returned to players.
2. Revenue Statistics, AM. GAMING ASS'N, [http://www.americangaming.org/Industry/factsheets/statistics\\_detail.cfv?id=7](http://www.americangaming.org/Industry/factsheets/statistics_detail.cfv?id=7) (last visited Jan. 22, 2010).
3. Unlawful Internet Gambling Enforcement Act of 2006, 31 U.S.C. §§ 5361–67 (2006).
4. *Id.*
5. *In re Baum*, 386 B.R. 649 (Bankr. N.D. Ohio 2008).
6. *Id.* at 656.
7. *Id.* at 651.
8. *Id.* at 659.

the United States. While the court ultimately applied the law correctly, this Note focuses on how the statute itself should be amended or repealed to avoid the undue burden it creates.

Section II of this Note will review the legal background that led up to the *Baum* decision. Section III will provide a detailed exposition of the case. Next, Section IV will offer analysis of the case, expanding upon the idea that the law itself is the real problem. Additionally, the analysis will propose a solution to the problematic statute.

## II. LEGAL BACKGROUND

Gaming has been regulated since the 1700's. This regulation has been primarily statutory, beginning with the Statute of Queen Anne and eventually leading to the Wire Act. The UIGEA is the most recent addition to the statutory scheme of gaming regulation.

### A. Early Statutory Law

The Statute of Queen Anne served as the basis of early American statutory law regarding enforcement of gambling debts.<sup>9</sup> Queen Anne of England signed the statute into law in 1710, and gambling debts have basically been unenforceable in all of the English-speaking world since.<sup>10</sup> Despite gaining independence from Great Britain, or the fact that much of the statute was subsequently repealed by English Parliament, many U.S. states adopted the Statute of Queen Anne, in one form or another.<sup>11</sup> Section One of the statute essentially made it illegal to collect any debt incurred as a result of knowingly lending money for the purposes of gambling.<sup>12</sup>

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9. 71 AM. JUR. PROOF OF FACTS 3D 193 § 2 (2009).

10. Nelson Rose, *Court Rules Internet Gambling is Not Legal*, U. OF NEV. LAS VEGAS, <http://gaming.unlv.edu/reading/rose73.html> (last updated Mar. 17, 2006).

11. AM. JUR. PROOF OF FACTS 3D, *supra* note 9, at § 2.

12. *Id.* (citing Statute of Queen Anne).

[F]rom and after the first day of May one thousand seven hundred and eleven all notes, bills, bonds, judgments, mortgages, or other securities or conveyances whatsoever given, granted, drawn, or entered into, or executed by any person or persons whatsoever where the whole or any part of the consideration of such conveyances or securities shall be for any money or other valuable thing whatsoever won by gaming or playing at cards, dice, tables, tennis, bowls, or other game or games whatsoever or by betting on the sides or hands of such as do game at any of the games aforesaid or for the reimbursing or repaying any money knowingly lent or advanced for such gaming or betting as aforesaid or lent or advanced at the time and place of such play to any person or persons so gaming or betting as aforesaid or that shall during such play, so play or bet shall be utterly void, frustrate, and of none effect to all intents and purposes

*Mordecai v. Dawkins* is an early example of the statute's application.<sup>13</sup> In 1856, the South Carolina Court of Appeals heard a case involving a person trying to reclaim money lent to another for the purposes of gambling.<sup>14</sup> The court applied its version of the Statute of Anne and determined that any security given as consideration for money lent for the purpose of gambling was void.<sup>15</sup> Further, the court stated that a void security did not convey any rights, so there could be no cause of action for recovery of the lent money.<sup>16</sup>

### B. Statutory Exceptions

Except for horseracing, gambling was illegal almost everywhere in the United States until the 20th century.<sup>17</sup> The early statutory laws regarding enforcement of gambling debts began changing once states started to legalize other forms of gambling.<sup>18</sup> As states progressively decided to allow gambling at land-based casinos, riverboat casinos, and casinos that were operated by federally recognized tribes on tribal land, they also began to build exceptions into the statutes which prohibited such actions.<sup>19</sup>

### C. *In re* Mastercard International Inc., Internet Gambling Litigation

The time between the legalization of various forms of gambling in the United States and 2001 was somewhat of a transitional period for statutory

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whatsoever any statute, law, or usage to the contrary thereof in any wise notwithstanding . . . .

*Id.*

13. *Mordecai v. Dawkins*, 43 S.C.L. 262, 1856 WL 3169 (S.C. Ct. App. 1856).
14. *Id.* at \*1.
15. *Id.* at \*3.
16. *Id.* at \*2.
17. AM. JUR. PROOF OF FACTS 3D, *supra* note 9, at § 1. The issues regarding the legality of horseracing are beyond the scope of this Note.
18. *Id.* at § 4.
19. *Id.* at § 1. See FLA. STAT. ANN. § 849.26 (West 2010) "Gambling Contracts Declared Void, Exceptions" (pari-mutuels or any gambling transaction expressly authorized by law); 720 ILL. COMP. STAT. 5/28-7 (West 2010) "Gambling Contracts Void," (except for legal riverboat gambling (d)); MINN. STAT. ANN. § 541.21 (West 2010) "Commitments for Gambling Debt Void" (except for specified legal gambling); MISS. CODE ANN. § 87-1-1 (West 2010) "Gambling Contracts Void"; MISS. CODE ANN. § 75-76-175 (West 2010) "Acceptance of Credit Instruments"; OHIO REV. CODE ANN. § 3763.01 (West 2010) "Gaming Contracts Void; Exceptions" (except charitable bingo and non-criminal gaming); S.D. CODIFIED LAWS § 53-9-2 (2010) "Gambling Contracts Void"; S.D. CODIFIED LAWS § 42-7B-55 (2010) "Certain Gambling Statutes Not Applicable"; VA. CODE ANN. § 11-14 (West 2010) "Gaming Contracts Void" (in 1998 an amendment exempted the state lottery from VA. CODE ANN. § 11-14); WASH. REV. CODE ANN. § 4.24.090 (West 2011) "Validity of Evidence of Gambling Debt," (void except for holder in due course); WIS. STAT. ANN. § 895.055 (West 2009) "Gaming Contracts Void" (except for specified legal gambling).

enforcement of gambling debts. As discussed in Section B, many exceptions to the early gambling statutes were emerging. Also, online gambling began to surface, which raised further questions of how old gambling statutes would apply to new technology. In 2001, however, a landmark case addressed three important federal statutes that many attorneys thought would continue to void the enforcement of online gambling debts. In this case, *In re MasterCard International Inc., Internet Gambling Litigation*,<sup>20</sup> the District Court for the Eastern District of Louisiana analyzed enforcement of online gambling debts with respect to the Racketeer Influenced and Corrupt Organizations Act (RICO), the Wire Act, and the Travel Act.<sup>21</sup>

This litigation began when online gamblers filed numerous class action suits in various district courts alleging that MasterCard International, Visa International, and several card-issuing banks interacted with internet casinos in violation of United States law.<sup>22</sup> Specifically, plaintiffs alleged that defendants' activities showed a pattern of racketeering in violation of the RICO statute.<sup>23</sup>

The Judicial Panel on Multidistrict Litigation transferred all of the cases to the Eastern District of Louisiana on March 1, 2000.<sup>24</sup> That court, on June 14, 2000, ordered the parties of two "test" cases to brief the court with respect to Federal Rules of Civil Procedure 12 and 19 regarding only federal law claims.<sup>25</sup> The court further ordered that all other cases in the multidistrict litigation be put on hold pending the resolution of the test cases.<sup>26</sup>

Larry Thompson and Lawrence Bradley, plaintiffs in the two test cases, used their credit cards to purchase credits with numerous online gambling websites.<sup>27</sup> Plaintiffs then used those credits to place wagers on the various websites.<sup>28</sup> Bradley wagered \$16,445 and was charged \$7,048 on his Visa credit card.<sup>29</sup> Thompson wagered \$1,520 and was charged \$1,510 on his MasterCard credit card.<sup>30</sup> Ultimately, the United States District Court for the Eastern District of Louisiana granted defendants' motions to dismiss for failure to state a claim upon which relief could be

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20. *In re Mastercard Int'l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d 468 (E.D. La. 2001).

21. Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §§ 1961–1968 (2006); Wire Act, 18 U.S.C. § 1084 (2006); Travel Act, 18 U.S.C. § 1952 (2006).

22. *Mastercard Int'l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d at 471.

23. *Id.* at 472; RICO §§ 1961–68.

24. *Mastercard Int'l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d at 471.

25. *Id.* at 471–72.

26. *Id.* at 472.

27. *Id.* at 474.

28. *Id.*

29. *Id.*

30. *Id.*

granted.<sup>31</sup> A year later, the Court of Appeals for the Fifth Circuit affirmed the ruling by the district court, adopting the majority of their analysis.<sup>32</sup>

### 1. *The Wire Act*

The first statute the district court addressed was the Wire Act, which states that those operating in the business of betting, and who knowingly use wire communications in interstate or foreign commerce to assist in the placement of bets or wagers on any sporting event or contest, shall be fined or imprisoned.<sup>33</sup> The plaintiffs argued that the Wire Act applied because the defendants assisted in the placement of wagers.<sup>34</sup>

The court first looked at the text of the statute, and found, reading it plainly, that the Act only prohibits wagers on sporting events or contests.<sup>35</sup> Further, the statute has a safe harbor provision which precludes criminal liability when information is transmitted in interstate or foreign commerce for use in news reporting of sporting events or contests “from a State or foreign country where betting on that sporting event or contest is legal into a State or foreign country in which such betting is legal.”<sup>36</sup> The court noted that both the rule and its exception “expressly qualify the nature of the gambling activity as that related to a ‘sporting event or contest.’”<sup>37</sup> The court even looked briefly at the legislative history surrounding the Act’s passage, particularly a statement by the House Judiciary Committee Chairman stating that “this particular bill involves the transmission of wagers or bets and layoffs on horse racing and other sporting events.”<sup>38</sup> Thus, wagers on games of skill or chance are not prohibited by the statute.<sup>39</sup>

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31. *Id.* at 497.

32. *In re Mastercard Int’l Inc.*, 313 F.3d 257 (5th Cir. 2002). The circuit court mostly adopted the lower court ruling, therefore this Note will focus on the district court opinion because it contains the vast majority of the factual information and legal analysis.

33. Wire Act, 18 U.S.C. § 1084(a) (2006).

Whoever being engaged in the business of betting or wagering knowingly uses a wire communication facility for the transmission in interstate or foreign commerce of bets or wagers or information assisting in the placing of bets or wagers on any sporting event or contest, or for the transmission of a wire communication which entitles the recipient to receive money or credit as a result of bets or wagers, or for information assisting in the placing of bets or wagers, shall be fined under this title or imprisoned not more than two years, or both.

*Id.*

34. *Mastercard Int’l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d at 480.

35. *Id.*

36. Wire Act, 18 U.S.C. § 1084(b).

37. *Mastercard Int’l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d at 480.

38. *Id.* at 480–81 (*citing* 107 CONG. REC. 16, 533 (1961)).

39. *Id.* at 480.

The court noted that plaintiffs failed to allege any sports-related gambling on the internet casinos.<sup>40</sup> Further, the court stated that plaintiffs' complaints were "extremely thorough."<sup>41</sup> The failure of plaintiffs to allege the specific games or types of games played was found to be a critical error in their complaints, because the type of games played would determine the legality of the gambling activity.<sup>42</sup> Therefore, plaintiffs' claim that defendants violated the Wire Act by assisting in the placement of wagers was not valid.<sup>43</sup> The Court of Appeals specifically stated their agreement "with the district court's statutory interpretation, its reading of the relevant case law, its summary of the relevant legislative history, and its conclusion."<sup>44</sup>

## 2. *The Travel Act*

The second statute the court addressed was the Travel Act, which makes it illegal to distribute the proceeds of any unlawful activity via interstate or foreign commerce.<sup>45</sup> The statute goes on to define "unlawful activity" as including, among other conduct, any business enterprise involving gambling in "violation of the laws of the State in which they are committed or of the United States."<sup>46</sup> The plaintiffs argued that the Travel Act applied because the defendants illegally distributed proceeds from their unlawful activity, as evidenced by the alleged violation by the defendants of the Wire Act, as discussed above.<sup>47</sup>

The court disposed of allegations under the Travel Act quickly.<sup>48</sup> The court had already found that defendants had not violated any state or U.S.

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40. *Id.*

41. *Id.*

42. *Id.*

43. *Id.*

44. *In re Mastercard Int'l Inc.*, 313 F.3d 257, 262 (5th Cir. 2002).

45. Travel Act, 18 U.S.C. § 1952(a) (2006).

Whoever travels in interstate or foreign commerce or uses the mail or any facility in interstate or foreign commerce, with intent to—

(1) distribute the proceeds of any unlawful activity; or (2) commit any crime of violence to further any unlawful activity; or (3) otherwise promote, manage, establish, carry on, or facilitate the promotion, management, establishment, or carrying on, of any unlawful activity, and thereafter performs or attempts to perform—

(A) an act described in paragraph (1) or (3) shall be fined under this title, imprisoned not more than 5 years, or both; or (B) an act described in paragraph (2) shall be fined under this title, imprisoned for not more than 20 years, or both, and if death results shall be imprisoned for any term of years or for life.

*Id.*

46. Travel Act 18 U.S.C. § 1952(b).

47. *Mastercard Int'l Inc., Internet Gambling Litig.* 132 F. Supp. 2d at 483.

48. *Id.*

law, including the Wire Act, as discussed above.<sup>49</sup> Because a violation of the Travel Act requires the violation of another state or federal law and defendants violated no other applicable laws, a cause of action did not exist under the Travel Act.<sup>50</sup>

### 3. RICO

To violate RICO, a plaintiff must prove the defendant engaged in a pattern of racketeering activity which is connected to the acquisition, establishment, conduct, or control of an enterprise.<sup>51</sup> “A pattern of racketeering activity requires two or more predicate acts and a demonstration that the racketeering predicates are related and amount to or pose a threat of continued criminal activity.”<sup>52</sup> Such acts may be either state or federal crimes.<sup>53</sup>

Trying to show a valid cause of action under RICO, the plaintiffs alleged violations of the Wire Act and the Travel Act as predicate acts.<sup>54</sup> The court, however, determined that plaintiffs failed to plead several of the required elements for a RICO claim.<sup>55</sup> As discussed above, plaintiffs did not commit any predicate acts under RICO.<sup>56</sup> Therefore, plaintiffs’ RICO claim was “such a legally flawed cause of action” it had to be dismissed.<sup>57</sup>

In sum, *Mastercard* had a major impact on the enforcement of gambling debts by addressing the three federal statutes that appeared to still apply to the growing issue of internet gambling. By ruling that the Wire Act was unenforceable against all forms of online gambling other than sports wagering, *Mastercard* essentially removed the ability to impose any federal sanctions on internet gambling. Since the Wire Act did not make online casinos unlawful, it would be nearly impossible to violate the Travel Act or RICO by engaging in online gambling. Congress quickly stepped in with a new answer to the problem.

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49. *Id.* at 482–83.

50. *Id.* at 483.

51. RICO, 18 U.S.C. § 1962 (2006).

52. *In re Mastercard Int’l Inc.*, 313 F.3d 257, 261 (5th Cir. 2002) (quoting *St. Paul Mercury Ins. Co. v. Williamson*, 224 F.3d 425, 441 (5th Cir. 2000)).

53. *Id.*

54. *Mastercard Int’l Inc., Internet Gambling Litig.* 132 F. Supp. 2d at 478.

55. *Id.* at 497.

56. See *Mastercard Int’l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d 468; *Mastercard Int’l Inc.*, 313 F.3d 257.

57. *Mastercard Int’l Inc., Internet Gambling Litig.* 132 F. Supp. 2d at 497.

## D. Unlawful Internet Gambling Enforcement Act of 2006

Soon after realizing the implications of *In re Mastercard International Inc., Internet Gambling Litigation*, Congress took action. Just four years after *Mastercard* was affirmed by the Fifth Circuit, Congress passed the Unlawful Internet Gambling Enforcement Act of 2006 (UIGEA).<sup>58</sup> While the statute itself became law on October 13, 2006, the final regulations were not released by the Federal Reserve Board and U.S. Department of Treasury until November 12, 2008.<sup>59</sup> The rules finally became effective on January 19, 2009, but non-exempt participants were not required to comply with those rules until December 1, 2009.<sup>60</sup> The long delay between passage of the statute and enforcement of the regulations is the result of political fears that the statute might be repealed.<sup>61</sup> Essentially, the statute makes it illegal for operators of “unlawful internet gambling” websites to accept payment for gambling services from any money or wire transfer, Automatic Clearing House (ACH) or Electronic Fund Transfer (EFT) system, check or draft drawn on a bank or financial institution, or any type of card, including credit cards and stored-value cards.<sup>62</sup> The regulations further require that covered institutions must identify and block all such restricted internet transactions.<sup>63</sup> This combination of quick Congressional action followed by slow-moving regulatory promulgation set the stage for *In re Baum*.

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58. UIGEA, 31 U.S.C. §§ 5361–67 (2006).

59. Maureen A. Young, *Recent Federal Initiatives in Privacy and Information Security*, 1 PRIVACY AND DATA SECURITY LAW INSTITUTE 487, 502 (Practicing Law Institute) (10th Annual Ed. June 2009).

60. *Id.*

61. *Id.*

62. UIGEA, 31 U.S.C. § 5363 (2006).

No person engaged in the business of betting or wagering may knowingly accept, in connection with the participation of another person in unlawful Internet gambling—(1) credit, or the proceeds of credit, extended to or on behalf of such other person (including credit extended through the use of a credit card); (2) an electronic fund transfer, or funds transmitted by or through a money transmitting business, or the proceeds of an electronic fund transfer or money transmitting service, from or on behalf of such other person; (3) any check, draft, or similar instrument which is drawn by or on behalf of such other person and is drawn on or payable at or through any financial institution; or (4) the proceeds of any other form of financial transaction, as the Secretary and the Board of Governors of the Federal Reserve System may jointly prescribe by regulation, which involves a financial institution as a payor or financial intermediary on behalf of or for the benefit of such other person.

*Id.*

63. 12 C.F.R. § 233.5 (2009).



### III. EXPOSITION OF *IN RE BAUM*

In the case of *In re Baum*, the United States Bankruptcy Court for the Northern District of Ohio examined the enforceability of electronic gambling debts acquired via credit card payments.<sup>64</sup> This Note will focus only on that issue, with respect to federal law, although the court also addressed issues regarding potential dishonesty or bad faith on the debtor's part, as well as the totality of the circumstances of debtor's financial situation.<sup>65</sup> The Bankruptcy Court concluded that debts incurred from gambling losses via electronic credit card payments which were made after October 13, 2006, were unenforceable under federal law.<sup>66</sup>

#### A. Facts and Procedure

Darlene K. Baum began gambling online for personal entertainment in June or July of 2006.<sup>67</sup> Soon, she began gambling for increasing amounts of money, which she financed via payments from her credit cards.<sup>68</sup> Baum would gamble before work in the mornings, return home to gamble during her lunch break, and continue gambling in the evenings after work.<sup>69</sup> After three or four months of this activity, Baum realized she had a gambling problem.<sup>70</sup>

Baum stopped gambling online and sought a counselor in November of 2006.<sup>71</sup> During her counseling, Baum cancelled her home internet access.<sup>72</sup> By the time Baum began counseling she had amassed substantial credit card debt from her online gambling activities.<sup>73</sup> Baum's personal statements and her Statement of Financial Affairs showed that she had accumulated approximately \$40,000 of debt gambling online.<sup>74</sup> Baum sought the advice of a friend, who was also an attorney, and began investigating debt consolidation services.<sup>75</sup> Baum checked with five services between November of 2006 and January of 2007, but determined that she could not afford the consolidated monthly loan payments.<sup>76</sup> She

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64. *In re Baum*, 386 B.R. 649 (Bankr. N.D. Ohio 2008).

65. *Id.* at 652.

66. *Id.* at 659.

67. *Id.* at 651.

68. *Id.*

69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.*

73. *Id.*

74. *Id.*

75. *Id.*

76. *Id.*

did not sign up for any of the consolidation services, but was told by the representative of one of them that she should consider filing for bankruptcy.<sup>77</sup> In February of 2007, Baum contacted her attorney friend and filed a Chapter 7 petition.<sup>78</sup>

This case appeared before the United States Bankruptcy Court for the Northern District of Ohio on September 10, 2007, when the U.S. Trustee (hereinafter “UST”) filed a Motion to Dismiss the Case for Abuse of Chapter 7.<sup>79</sup> On September 20, 2007, Baum filed an objection to the motion.<sup>80</sup> Two months later, on November 20, 2007, the court held a motion hearing.<sup>81</sup> UST argued, in its brief and at the hearing, that Baum’s attempt to use Chapter 7 to discharge her obligations to her creditors amounted to bad faith or a dishonest relationship.<sup>82</sup> Either way, UST argued, Baum’s claim warranted dismissal for abuse of Chapter 7.<sup>83</sup> The court took the matter under advisement and gave the parties until November 27, 2007 to file additional briefs, but neither did.<sup>84</sup>

#### B. Opinion of the Court

The United States Bankruptcy Court for the Northern District of Ohio concluded that UST failed to meet the required burden, and therefore denied its Motion to Dismiss.<sup>85</sup> The court used a statutory provision in determining that Baum’s claim was not abusive. First, the court followed 11 U.S.C. § 707(c)(3)(A) in asking if any bad faith or dishonesty with creditors had been demonstrated by Baum.<sup>86</sup> Second, the court asked if the totality of the circumstances of Baum’s financial situation evidenced abuse under 11 U.S.C. §707(c)(3)(B).<sup>87</sup> Answering both questions “no,” the court moved to whether or not gambling debts are enforceable.

The court raised the issue of enforceability of gambling debts *sua sponte*.<sup>88</sup> Although neither party in the case briefed the issue and no fact-finding was done, the court was “compelled to address the issue because it raise[d] threshold questions that should have been addressed before

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77. *Id.*

78. *Id.*

79. *Id.*

80. *Id.*

81. *Id.*

82. *Id.* at 651–52.

83. *Id.* at 652.

84. *Id.* at 651.

85. *Id.* at 652.

86. *Id.*

87. *Id.* See *In re Krohn*, 886 F.2d 123 (6th Cir. 1989).

88. *Baum*, 386 B.R. at 656.

reaching the issues of bad faith and dishonesty with creditors.”<sup>89</sup> The court first addressed the issue under state law, stating that “[c]ontracts in support of gambling debts are void under Ohio Rev. Code § 3763.01.”<sup>90</sup> The court further noted the state’s “long-standing public policy against witnessing its citizens plunge headlong into debt by gambling on credit.”<sup>91</sup> Thus, the court determined that debts incurred from gambling activity were unenforceable under Ohio law.<sup>92</sup>

Next, the court recognized that, due to the passage of the UIGEA,<sup>93</sup> federal law was also applicable.<sup>94</sup> The court spelled out some of the statute’s provisions, making particular note of § 5365(a),<sup>95</sup> which provides that “[i]n addition to any other remedy under current law, the district courts of the United States shall have original and exclusive jurisdiction to prevent and restrain restricted transactions by issuing appropriate orders in accordance with this section, regardless of whether a prosecution has been initiated under this subchapter.”<sup>96</sup> Therefore, the court, exercising its “original and exclusive jurisdiction,” found that gambling debts “incurred via electronic credit card payments after October 13, 2006, are unenforceable under [federal law].”<sup>97</sup>

In sum, the court held that gambling debts are not enforceable under state or federal law.<sup>98</sup> Further, the court suggested that the issue of a debt’s enforceability should be raised prior to any issue dealing with bad faith or dishonesty on the part of a debtor.<sup>99</sup> Because “[v]oid or unenforceable debts cannot legally form the basis of a motion to dismiss for abuse of Chapter 7,”<sup>100</sup> the UST’s Motion to Dismiss was denied.<sup>101</sup>

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89. *Id.*

90. *Id.*

(A) All promises, agreements, notes, bills, bonds, or other contracts, mortgages, or other securities, when the whole or part of the consideration thereof is for money or other valuable thing won or lost, laid, staked, or betted at or upon a game of any kind, or upon a horse race or cockfights, sport or pastime, or on a wager, or for the repayment of money lent or advanced at the time of a game, play, or wager, for the purpose of being laid, betted, staked, or wagered, are void. (B) Sections 3763.01 to 3763.08 of the Revised Code do not apply to bingo as defined in section 2915.01 of the Revised Code or to any game of chance that is not subject to criminal penalties under section 2915.02 of the Revised Code.

OHIO REV.CODE § 3763.01 (2009).

91. *Baum*, 386 B.R. at 658 (quoting *In re Jafari* 378 B.R. 575 (Bankr. W.D. Wis. 2007)).

92. *Id.* at 659.

93. UIGEA, 18 U.S.C. §§ 5361–67 (2006).

94. *Baum*, 386 B.R. at 659.

95. *Id.*

96. *Id.* (citing § 5365(a)).

97. *Id.*

98. *Id.*

99. *Id.* at 656.

100. *Id.*

#### IV. ANALYSIS

*Baum* laid the groundwork for judicial application of the UIGEA. More importantly, the *Baum* court illustrated the inherent flaws of the statute, even as it correctly applied the law to the facts at hand. This section will discuss why the United States Bankruptcy Court for the Northern District of Ohio reached the correct conclusion and where the decision fits with respect to prior law. Further, this section addresses the impact the *Baum* decision has on the future and proposes a less-burdensome alternative to the UIGEA.

##### A. The *Baum* Court Reached the Correct Decision

Although the UIGEA places an unnecessary burden on American financial institutions, the *Baum* decision was reached in accordance with the newly-enacted statute. As the case was one of first impression, there was no precedent for the court to follow in applying the statute. The court was also unable to employ the guidance offered by previous analysis regarding similar issues under earlier statutory schemes, since they were no longer relevant. Therefore, the court had only the plain text of the statute at its disposal. The court did not consider it necessary to interpret the statute, but rather cited the statutory text plainly in ruling that electronic gambling debts incurred via credit card transactions were not enforceable.<sup>102</sup> With no other recourse and no meaningful argument that the process followed by the *Baum* court was erroneous, the decision reached was legally correct.

##### B. *Baum*'s Place in Gaming Law

As discussed in Section II, the law pertaining to enforcement of gambling debts in America has undergone numerous changes. Eventually,

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101. *Id.* at 659.

102. *Id.*

No person engaged in the business of betting or wagering may knowingly accept, in connection with the participation of another person in unlawful Internet gambling—(1) credit, or the proceeds of credit, extended to or on behalf of such other person (including credit extended through the use of a credit card); (2) an electronic fund transfer, or funds transmitted by or through a money transmitting business, or the proceeds of an electronic fund transfer or money transmitting service, from or on behalf of such other person; (3) any check, draft, or similar instrument which is drawn by or on behalf of such other person and is drawn on or payable at or through any financial institution; or (4) the proceeds of any other form of financial transaction, as the Secretary and the Board of Governors of the Federal Reserve System may jointly prescribe by regulation, which involves a financial institution as a payor or financial intermediary on behalf of or for the benefit of such other person.

UIGEA, 31 U.S.C. § 5363 (2006).

the *Mastercard* decision effectively made it impossible to violate federal law by engaging in such online gambling.<sup>103</sup> After *Mastercard*, American citizens and online casinos enjoyed a brief period of unencumbered activity, until the UIGEA was finally passed in 2006.<sup>104</sup> Shortly thereafter, *Baum* was decided, and became the first case to apply the new law.<sup>105</sup> Until that time, American gaming law had seen a progressive evolution from strict prohibition to accepting regulation. The *Baum* court, because its hands were tied by the UIGEA, abruptly halted that evolution. In fact, some of the progression has been reverted, because once-legal activity, online gambling not involving sports, is now technically against federal law. Not only did the UIGEA end the forward movement of American gaming law, but it also forced a backward step away from the most recent gain. Thus, the UIGEA forced *Baum* into an unsavory position in American gaming law history, where it is known as the decision that prohibited progress.

### C. *Baum*'s Effect on the Future of Online Gambling

Aside from the effects *Baum* had on gaming law's progressive legal movement, the decision also had a major impact on the future of online gambling. The UIGEA does not address the issue of online gambling adequately and creates an undue burden on American companies. Additionally, the statute *Baum* was forced to apply does not sufficiently define the type of activities that are illegal, thus no clear legal standard is available to put potential violators on notice.

#### 1. *Baum*'s Burden on American Financial Institutions

As discussed in Section II, the UIGEA effectively bans the use of U.S. payment systems for processing illegal online gambling transactions.<sup>106</sup> Like the statute, the regulations promulgated under the UIGEA do not allow criminal action to be taken against individuals who gamble online.<sup>107</sup> In fact, the regulations do not even apply to institutions or transactions outside of the United States.<sup>108</sup> Therefore, the entire burden of enforcement falls upon U.S. financial institutions. Financial service companies that are subject to U.S. jurisdiction and participate in any of the five named payment systems must implement policies that have a reasonable chance of

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103. *In re Mastercard Int'l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d 468 (E.D. La. 2001).

104. UIGEA, 31 U.S.C. §§ 5361–67.

105. *Baum*, 386 B.R. 649.

106. UIGEA, 31 U.S.C. §§ 5361–67.

107. Young, *supra* note 59, at 504.

108. *Id.*

preventing the processing of prohibited online gambling transactions.<sup>109</sup> Those payment systems consist of: (a) ACH systems, (b) card payments, (c) check collection, (d) money transmission, and (e) wire transfers.<sup>110</sup>

As previously noted, *Baum*'s application of the UIGEA was correct and well-reasoned, especially considering it was a case of first impression. The statute itself, however, was not well written, as it creates an absurd situation where individual gamblers and offshore internet casinos have free reign and American financial institutions are caught in the middle. *Baum* clearly demonstrated this problem by ruling that the UST could not force Darlene Baum to pay her gambling debts, thus footing the credit card company and the U.S. government with the bill for Baum's irresponsible behavior.<sup>111</sup> Thus, the financial institutions are being forced to become policing entities, or else face the wrath of the government. American citizens have no incentive to stop internet gambling on credit, because, if the financial institution does not prevent the transaction, *Baum* tells individuals they are not liable for any debt, either to the credit card company or the U.S. government. Furthermore, offshore casinos have no incentive to stop seeking the business of American gamblers because the U.S. laws do not reach them. While they will certainly see a drop in revenue from U.S. gamblers, any transactions that slip through the cracks in the financial institutions' gambling-transaction-blocking methods are additional bonuses for those companies. Therefore, parties on both ends of the gambling experience have a sure bet. The parties cannot be held liable for money lost while gambling online, and money won is akin to a windfall. The only parties being dealt a bad hand are American financial institutions, who are charged with stopping such gambling transactions from taking place. Not only must those institutions eat any losses that occur to credit cards they hold due to their lack of ability to recover from individuals, but they are also subject to potential punishment from the U.S. government under the Gramm-Leach-Bliley Act, the Commodity Exchange Act, and the Federal Trade Commission.<sup>112</sup>

Although U.S. law does not reach internet casinos based outside the country, American financial institutions must implement policies that address domestic and international transactions.<sup>113</sup> Thus, U.S. institutions must know their foreign financial customers and what types of transactions they are conducting with the U.S. institution.<sup>114</sup> Responsibility for

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109. *Id.* at 503.

110. 12 C.F.R. § 233.3 (2009).

111. *In re Baum*, 386 B.R. 649 (Bankr. N.D. Ohio 2008).

112. 12 C.F.R. § 233.7 (2009).

113. Young, *supra* note 59, at 504.

114. *Id.*

compliance rests with the first U.S. institution that receives payment from a transaction by a foreign financial institution.<sup>115</sup> So, while the law itself does not reach outside American borders, it does impose a duty upon American financial institutions to block any transactions it receives from foreign entities that pertain to illegal internet gambling. The regulations do provide some “safe harbor” examples, which ensure that an institution following the example set of procedures will be deemed compliant with the law.<sup>116</sup> These example procedures are very comprehensive in scope, and therefore quite costly to implement. In fact, rulemaking agencies estimate that the additional record keeping burden of these new policies on covered financial institutions will add up to about one million hours.<sup>117</sup> Furthermore, over 12,000 small businesses are subject to these new, costly regulations.<sup>118</sup> *Baum’s* burden on American financial institutions is extensive, expensive, and explicit.

## 2. *Baum’s Statement of Statutory Ambiguity*

*Baum’s* application of the UIGEA demonstrated another major problem by revealing the statute’s ambiguity. The statute bans “unlawful internet gambling,” yet never fully explains what that means.<sup>119</sup> The regulations promulgated under the Act define “unlawful internet gambling” as placing, receiving, or otherwise knowingly transmitting a bet by any means that involves the Internet where such bet is unlawful under any applicable federal or state law in the state in which the bet is placed, received, or made.<sup>120</sup> Numerous issues surround the legality of different types of internet betting, which demonstrate “how the phrase ‘unlawful under any applicable federal or state law’ renders UIGEA ineffective.”<sup>121</sup> *Mastercard* removed non-sports online betting from the ranks of federally criminal activities, which suggests that the UIGEA can only apply where online gambling activity is illegal by some state law.<sup>122</sup> Some argue that, in effect, the law maintains the status quo because it does not define, exactly, what forms of online betting are legal or illegal.<sup>123</sup> Others are concerned

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115. *Id.*

116. 12 C.F.R. § 233.6 (2009).

117. *Federal Issues*, AM. GAMING ASS’N, [http://www.americangaming.org/federal\\_issues/issues.cfv?ID=9](http://www.americangaming.org/federal_issues/issues.cfv?ID=9) (last visited Jan. 22, 2010).

118. *Id.*

119. UIGEA, 31 U.S.C. § 5363 (2006).

120. 12 C.F.R. § 233.2(bb) (2009).

121. Jon Feldon, Comment, *Bluffing? The Legislative Response to Internet Gambling*, WASH. C. OF L. CRIM. L. BRIEF, Fall 2006, at 13, 13.

122. See *In re Mastercard Int’l Inc.*, 313 F.3d 257 (5th Cir. 2002).

123. AM. GAMING ASS’N, *supra* note 117.

the statute creates even more questions and ambiguity than it solves.<sup>124</sup> Online casinos still must guess whether or not their activities will be considered legal, but now enforcement rests with American financial institutions, rather than the government or judicial system. Some experts believe the result will be the death of American internet gambling, while others are sure the cessation will be only temporary, with new companies rushing to fill the void left by emerging legal loopholes.<sup>125</sup>

In a broad sense, the status quo does remain, because the overall level of uncertainty regarding what online gambling is legal or illegal has not changed. New, specific questions regarding enforcement have been created for financial institutions, however, which further clouds an already murky issue. *Baum*'s ruling saddled financial institutions with the burden, while allowing citizens like Darlene Baum to gamble away, without regard to risk or the consequences of losing. Further, online casinos have a similar incentive to continue operation, because doing so cannot result in any penalty, but only possible revenue from gamblers. The result is a perverse game of seesaw with American citizens on one end, offshore internet casinos on the other, and American financial institutions forced to be the fulcrum. While the length of the game is uncertain, the conclusion is inevitable. One side will find ways to work the system for a while, until the financial institutions get wise and attempt to move the focal point. Then, the other side will suddenly have new loopholes to exploit, and will benefit for a time. As financial institutions struggle to find the correct answer to their newly-created enforcement problem, momentum and benefit will shift back and forth between online gamblers and internet casinos. Eventually, both sides will have generated enough leverage over the system that no position will exist where the fulcrum can sustain any semblance of balance and the plank will snap. Therefore, while shifting the burden to a party that can be monitored, *Baum* has not succeeded in stopping online gambling, overall. A short-term cessation will occur while casinos and gamblers test the weight of the new system, but eventually both sides will be back in full swing, and internet gambling will resume.

#### D. Legalized Regulation is an Efficient, Effective Alternative to Prohibition

*Baum* clearly highlights the many problems inherent in the UIGEA. Even if the statute were more clearly worded and definite, though, absolute prohibition of online gambling is not the best route. Offshore internet

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124. Feldon, *supra* note 121, at 13.

125. *Id.* at 14.



casino revenue for 2008 was estimated to be \$5.9 billion from players in the United States and \$21 billion from players all over the world.<sup>126</sup> Banning online gambling, even in a roundabout manner, is inefficient. Moreover, *Baum*'s method of attempting to block online gambling, forcing American financial institutions to block transactions involving such activity, is costly to American businesses. Since banning online gambling outright faced so much opposition, the legislature decided to ban the use of financial instruments for the purposes of illegal online gambling.<sup>127</sup> Thus, American business must bear the burdens of this costly prohibition, while individuals and online casinos are free to act as they please. *Baum* shows how this paternalistic approach is short-sighted and poorly designed. By allowing Darlene Baum to gamble online until she had accumulated vast debt, and then cancelling her obligation to pay her credit card company, the *Baum* court forced the card-issuing company to absorb the loss itself. The cost does not stop there. The same company forced to absorb the loss must also implement procedures to ensure that the same activity does not happen again in the future. Darlene Baum, on the other hand, can obtain another credit card from a different company and repeat her prior conduct, if she wishes, without fear of punishment. The goal of protecting unwary American citizens from slipping into the jaws of gambling addiction is laudable, but forcing American businesses to fund the ends toward that mean is not. Thus, the *Baum* ruling not only imposes additional costs on American institutions, but also misses out on a major opportunity for increased tax revenue.

*Baum* was forced to apply the UIGEA, and in doing so revealed that the current statutory scheme is inferior. The effects realized by the *Baum* decision suggest that the UIGEA should be amended or repealed such that online gambling is legally regulated and taxed, rather than incidentally prohibited. The current statute is a poor, expensive, and impractical attempt at stopping online gambling in the United States. In fact, all the *Baum* decision accomplished was to impose a new, costly, inefficient burden on American financial institutions. In the wake of *Baum*, the law creates new incentives for financial institutions to prohibit certain types of transactions. Those institutions are forced to enact strict, costly new measures to be certain that all prohibited transactions are, in fact, blocked. Instead of creating expensive new incentives for financial institutions to implement additional procedures, gaming law should work to remove the incentive for individual gamblers and the online casinos to engage in illegal gambling. *Baum* does not accomplish that. Legalizing most types of online gambling,

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126. *Industry Information*, AM. GAMING ASS'N, [http://www.americangaming.org/Industry/factsheets/issues\\_detail.cfv?id=17](http://www.americangaming.org/Industry/factsheets/issues_detail.cfv?id=17) (last visited Jan. 22, 2010).

127. *Id.*

and then strictly regulating them, would. The basic scheme for doing so is already established. Land-based, riverboat, and Indian tribal casinos are strictly regulated in the United States. It would not be very difficult or costly to follow the lead of those industries and create a program governing the application and licensing of internet casinos.

In 2008, twelve states had legal, regulated commercial casinos, and contributed \$5.66 billion in tax revenue to local and state governments.<sup>128</sup> Those tax dollars supported education, economic development, public safety, and infrastructure improvements.<sup>129</sup> Under *Baum*, state and federal governments are unable to benefit from taxes on the \$21 billion internet gaming industry, which is short-sighted, costly, and inefficient.

## V. CONCLUSION

*Baum* correctly applied the UIGEA by ruling that debts incurred from gambling losses via electronic credit card payments were unenforceable under federal law. The case illuminates the problematic issues with the current statutory scheme. Applying the UIGEA, the *Baum* decision created extreme burdens on American financial institutions. Aside from forcing such institutions to enact costly new policies of enforcement, the statute is also vague and difficult to apply due to definitional ambiguities. After *Baum*, financial institutions will be forced to strictly apply their policies due to inadequate definitions concerning what type of online gambling is illegal. Instead of imposing such burdens on the middleman financial institutions in lieu of the actual parties involved in gambling activity, the internet gaming industry should be legalized and regulated. Such regulation would resolve all of the issues created by *Baum*, and also procure additional tax revenue for the state and federal governments.

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128. Tax Payments of Commercial Casinos, AM. GAMING ASS'N, [http://www.americangaming.org/Industry/factsheets/statistics\\_detail.cfv?id=10](http://www.americangaming.org/Industry/factsheets/statistics_detail.cfv?id=10) (last visited Jan. 22, 2010). The states included in the total were Colorado, Illinois, Indiana, Iowa, Louisiana, Michigan, Mississippi, Missouri, Nevada, New Jersey, Pennsylvania, and South Dakota.

129. *Id.*