OF BOOKIES AND BROKERS: ARE SPORTS FUTURES GAMBLING OR INVESTING, AND DOES IT EVEN MATTER?

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INTRODUCTION

You are in the midst of a trading pit on the floor of the exchange. In the controlled chaos around you, other buyers and sellers are shouting and raising their hands to get the trader's attention. The trader acknowledges the seller on your left and buyer behind you, and all three scribble furiously in their notepads. You are anxious to buy your contracts because the price is rising and reducing your prospective return. The trader shouts, "Redskins at twenty," you raise your hand, he points to you, you write down the trade, and move off to trade in the Cowboys pit.

The exchange just described is a form of information market. Information markets facilitate the trading of contracts whose values depend on the occurrence of an uncertain event.[1] A sports future is such a contract in which the uncertain event is the outcome of a sporting event (e.g., football or baseball game). Those who successfully predict the future earn positive profits in these markets. Many academics believe that these profits encourage traders to find and act on superior information, and that the market price will reflect that information to give an accurate prediction of an event's outcome.[2] There are more than twenty-three information markets operating on the internet, not all of which trade on sports.[3] Empirical evi-

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1 Robert W. Hahn & Paul C. Tetlock, *A New Approach for Regulating Information Markets*, 29 J. REG. ECON. 265, 265 (2006).

2 *Id.* at 266; *see also CBS Sunday Morning: The Crowd Knows Best* (CBS television broadcast Jan. 8, 2006), *available at* http://www.cbsnews.com/stories/2006/01/08/sunday/printable1185604.shtml (quoting Harvard Business School Professor Anita Elberse as saying, "One expert will never know as much as a group of people").

3 Hahn & Tetlock, *supra* note 1, at 266; *cf.* Robin Hanson, *Could Gambling Save Science? Encouraging an Honest Consensus*, *in* GAMBLING AND COMMERCIAL GAMING: ESSAYS IN BUSINESS, ECONOMICS, PHILOSOPHY, AND SCIENCE 399 (W. Eadington & J. Cornelius eds., 1992) (proposing an

dence shows that such markets can be extremely accurate predictors of future events.[4]

Despite widespread academic and empirical support,[5] the United States' prohibitory gambling regime has prevented all but one real-money information market from operating domestically.[6] This regime stems from, inter alia: The Wire Act, which makes it illegal to use a wire communication facility to transmit sports-gambling information;[7] the Department of Justice's position that The Wire Act prohibits all online gambling, even non-sports gambling;[8] and a recent Congressional attempt to modernize The Wire Act and codify the Department of Justice's position.[9] Although it is not clear that information markets could be prosecuted under the present version of The Wire Act, the United States' ambiguous legal environment is more hostile than that of at least sixty-four other countries, including

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"idea futures" market in which one bets on the future settlement of a present scientific controversy). For examples of online information markets, see Hollywood Stock Exchange, http://www.hollywoodstocke xchange.com (trading on movies and movie stars); NewsFutures, http://us.newsfutures.com (trading on news events); Tradesports, http://www.tradesports.com (trading on sports, politics and weather).

4 *See infra* Part I.B.

5 *See, e.g.*, Hahn & Tetlock, *supra* note 1, at 266-67; *see also* Michael Abramowicz, *Information Markets, Administrative Decisionmaking, and Cost-Benefit Analysis,* 71 U. CHI. L. REV. 933, 936 (2004) ("[S]tudies indicate that information markets are generally superior to other forecasting tools, such as polls, because information markets aggregate various types of information and a range of individuals' predictions."); Robin Hanson et al., *Information Aggregation and Manipulation in an Experimental Market*, 60 J. ECON. & BEHAV. ORG. 449, 458 (2006). *But see* Steven Pearlstein, *Misplacing Trust in the Markets*, WASH. POST, July 30, 2003, at E1; Press Release, Senator Ron Wyden & Senator Byron Dorgan, Wyden, Dorgan Call For Immediate Halt to Tax-Funded 'Terror Market' Scheme, (July 28, 2003), *available at* http://wyden.senate.gov/media/2003/07282003_terrormarket.html.

6 Hahn & Tetlock, *supra* note 1, at 269-70. The only legal and continuous real-money information market in the United States, the Iowa Electronics Market, is operated by the University of Iowa under a non-interference letter from the CFTC. Abramowicz, *supra* note 5, at 944. For more information on the Iowa Electronics Market, see About the Iowa Electronic Markets, http://www.biz.uiowa.edu/iem/
about.

7 18 U.S.C. § 1084(a) (2000); *see also In re* Mastercard Int'l Inc. Internet Gambling Litig., 313 F.3d 257, 262-63 (5th Cir. 2002) (holding The Wire Act prohibits sports gambling on the internet).

8 Christine Hurt, *Regulating Public Morals and Private Markets: Online Securities Trading, Internet Gambling and the Speculation Paradox*, 86 B.U. L. REV. 371, 414 (2006) (explaining that the Department of Justice believes The Wire Act prohibits all online gambling). *But see Mastercard*, 313 F.3d at 263 (rejecting the Department of Justice's position and holding The Wire Act does not apply to non-sports gambling over the internet).

9 Internet Gambling Prohibition and Enforcement Act, H.R. 4411, 109th Cong. (as placed on Senate calendar, July 13, 2006); *see also* Press Release, Representative Pete Hoekstra, Hoekstra Votes to Curb Online Gambling (July 11, 2006), *available at* http://hoekstra.house.gov/News/DocumentSingle .aspx?DocumentID=46833 ("The [Internet Gambling Prohibition and Enforcement Act] updates the 1961 Wire Act to unambiguously apply to Internet gambling, not only sports bets placed over the telephone.").

Great Britain, which clearly allow and regulate online gambling and sports futures.[10] Because the internet allows offshore information markets access to American consumers without the threat of criminal prosecution, even the specter of prosecution under The Wire Act is more than enough to prevent information markets from locating domestically.[11] Therefore, such a regime keeps all information markets offshore, but fails to prevent American consumers from participating in those markets. This ineffective policy is symptomatic of the United States government's approach to online gambling generally. It is estimated that 80% of all money wagered online comes from the United States, and that the United States would have collected $1.2 billion in taxes had online gambling been legal in 2004.[12] These results should call into question a regulatory regime predicated on The Wire Act, which was drafted three decades before internet use was commonplace.

The Wire Act is representative of an attempt in American law to categorize speculative activities into investing or gambling, in order to regulate the former and prohibit the latter. Although many have maligned such a distinction, sports futures provide a unique opportunity to expose the inequities of this dichotomy because they have elements traditionally associated with both gambling and investing: their value is determined by the outcome of a sporting event; and their form is that of a futures contract, an investment vehicle regulated by the Commodity Futures Trading Commission ("CFTC").

This Comment argues that any attempt to distinguish categorically between investing and gambling is unprincipled and unworkable, and the prevailing regime predicated on that philosophy should be abandoned. A proper analysis, weighing the costs and benefits of sports futures, shows they should be regulated rather than prohibited. Part I describes futures and information markets. Part II shows that sports futures are both gambling and investing under the traditional gambling-investing dichotomy and argues that such a dual classification proves that the dichotomy is unprinci-

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10 *60 Minutes: I-Gaming: Illegal and Thriving* (CBS television broadcast Nov. 20, 2005), *available at* http://www.cbsnews.com/stories/2005/11/17/60minutes/main1052420.shtml?CMP=ILC-Search Stories [hereinafter *60 Minutes*]. Sixty-four may be conservative, since some claim that as many as eighty countries permit online gambling. TelecomWeb, *New Shooter: House Passes Online Gambling Dice to Senate*, July 12, 2006, *available at* http://www.telecomweb.com/tnd/18058.html [hereinafter TelecomWeb] (noting that "about 80 countries and jurisdictions" regulate rather than prohibit internet gambling).

11 One prominent online sports futures market gets 33-40% of its business from the United States. Press Release, Commodity Futures Trading Commission, U.S. Commodity Futures Trading Commission Assesses Penalties Against Irish Company Trade Exchange Network Limited For Offering Illegal Commodity Option Contracts (Oct. 4, 2005), *available at* http://www.cftc.gov/opa/enf05/opa5124-05.htm [hereinafter Press Release, CFTC].

12 *60 Minutes*, *supra* note 10.

pled and should be abandoned. Part II also analyzes existing explanations for the creation of the dichotomy, and offers an explanation for its persistence. Part III applies The Wire Act,[13] the Federal Aiding and Abetting statute,[14] and CFTC regulations to sports futures to show that even the regime spawned by the gambling-investing dichotomy cannot distinguish between the two activities.[15] Lastly, Part IV demonstrates that sports futures are at least as beneficial to society as online investing, which is already legal, and that sports futures should accordingly be legalized.

I. FUTURES MARKETS AND INFORMATION MARKETS

There are numerous examples of information markets outperforming other forecasting mechanisms.[16] The use of real-money markets in the United States has been almost non-existent,[17] however, because notwithstanding their similarity to futures markets, many consider them too close to gambling.[18] To evaluate the legitimacy of that criticism, an understanding of futures and information markets is necessary. This part describes both futures and information markets.

A. *Futures Markets*

Futures contracts are used to hedge and manage risk.[19] The easiest way to understand a futures contract is to first understand forward and spot contracts. Spot contracts are the agreements that people enter into every day: agreements for present payment and delivery.[20] Forward contracts, in contrast, are agreements on a price to be paid for delivery in the future.[21] In a

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13 18 U.S.C. § 1084(a) (2000).

14 18 U.S.C. § 2 (2000).

15 17 C.F.R. §§ 1.1-.70 (2006).

16 *See infra* notes 42-45 and accompanying text; *see also* Robin Hanson, *Foul Play in Information Markets*, *in* INFORMATION MARKETS: A NEW WAY OF MAKING DECISIONS 126 (Robert Hahn & Paul Tetlock eds., 2006) [hereinafter *Foul Play*] ("Orange juice futures improve on National Weather Service forecasts, horse race markets beat horse race experts, Oscar markets beat columnist forecasts, gas demand markets beat gas demand experts, stock markets beat the official NASA panel at fingering the guilty company in the Challenger accident, election markets beat national opinion polls, and corporate sales markets beat official corporate forecasts.") (citations omitted).

17 Abramowicz, *supra* note 5, at 944.

18 *See, e.g.*, Hahn & Tetlock, *supra* note 1.

19 Commodity Futures Trading Commission, The Economic Purpose of Futures Markets (Feb. 3, 2006), http://www.cftc.gov/opa/brochures/opaeconpurp.htm [hereinafter Futures Markets].

20 *Id.*

21 *Id.*

forward contact, the seller agrees to deliver a commodity, say wheat, at a designated time, and the buyer agrees to pay at delivery a price determined at the time of contracting.[22] Forward contracts also contain specialized terms, like place of delivery, specially bargained-for by the parties to effectuate a transfer of merchandise.[23] With these specialized terms, the only way to get out of a forward contract without breach is to have the other party agree to cancel the contract.[24]

Futures contracts are similar to forward contracts in that they are also for future delivery of a commodity at a pre-arranged price.[25] Futures contracts, however, have standard features so they can be traded on an exchange.[26] These standard features allow a trader to exit a contract by purchasing an offsetting contract[27] that is readily available on the exchange.[28] The ability to offset the contract allows traders in futures contracts to speculate on prices without ever having to deliver or accept the underlying goods.[29] Speculating is simply making a bet on the movement of the price by purchasing a contract and then purchasing an offsetting contract to pocket (or pay) the difference.[30]

Unlike traditional debt and equity markets, where all investors can be winners if the market is rising, there is always a winner and a loser to each futures contract.[31] Futures contracts are only capable of wealth-transfer, which is essentially moving money from the loser to the winner.[32] This is called a zero-sum activity because when one side's losses are subtracted

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22 *Id.*

23 *See id.*

24 *See id.*

25 *See* Futures Markets, *supra* note 19.

26 *Id.*

27 *Id.* An offsetting contract is a contract requiring the opposite action to the contract currently owned. For example, if A owned a put contract (requiring him to sell) 100 bushels of wheat, the offsetting contract would be a call contract (requiring him to buy) 100 bushels of wheat. Concededly, it is not apparent how A has exited the market since it appears that he still is obligated to buy 100 bushels from one trader and sell those 100 to someone else. The answer is that all futures contracts are considered to be traded with a clearing organization (the market), and so A has effectively agreed to buy 100 bushels from the same party that he was previously promised to sell 100 bushels. Furthermore, since all the contracts have standardized features (time, manner, location of delivery, etc.), there are no extraneous obligations remaining after the offsetting contract is purchased. Therefore, after buying the call contract, A no longer has any obligation to buy or sell anything and has effectively exited the contract.

28 Id.

29 *Id.*

30 *Id.*

31 Thomas Lee Hazen, *Rational Investments, Speculation, or Gambling?—Derivatives Securities and Financial Futures and Their Effect on the Underlying Capital Markets*, 86 NW. U. L. REV. 987, 1006 (1992).

32 *Id.*; Steven D. Levitt, *Why Are Gambling Markets Organised So Differently From Financial Markets?* 114 ECON. J. 223, 223 (2004).

from the other's winnings the result is zero. However, futures markets involve transaction costs in the form of brokerage fees, and after subtracting these from an already zero-sum activity, futures contracts become a negative-sum activity. [33] This means that the investors collectively lose money on each trade. [34]

Notwithstanding the fact that traders lose in the aggregate, there are reasons for people to trade futures contracts. The primary purpose of futures contracts is to allow people to avoid the risk of price fluctuation in the underlying asset.[35] For example, Farmer Brown could sell contracts at the time of planting to lock-in his sale price at harvest time.[36] If Farmer Brown wanted to sell his wheat at the current price of $10.00 per bushel, he would need to buy a put contract (obligating him to sell at that price) for each bushel he expected to produce.[37] If the price declined to $9.00 at harvest, he would still have his buyer at $10.00.[38] Conversely, if the price rose to $11.00, he would still have to sell his wheat at $10.00 under the contracts.[39] Even when Farmer Brown is forced to sell for less than the market price, however, he benefits by not being forced to speculate on crop prices,[40] and he can focus on growing crops.[41]

B. *Information Markets*

The preceding discussion of futures markets provides a background with which to compare information markets and sports futures. This subpart provides background on information markets, including descriptions of a generic information market and a specific online information market that trades sports futures.

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33 Hazen, *supra* note 31, at 1006.

34 See *id.*

35 Speculation also plays a major role in futures contracts, but the CFTC maintains that their primary purpose is for hedging. Futures Markets, *supra* note 19.

36 *Id.*

37 *Id.*

38 *Id.* This may be an oversimplification, since it might be easier for a farmer in Oklahoma to buy offsetting call contracts at harvest at $9.00, pocketing $1.00 per contract, and then sell the wheat locally for $9.00 (totaling $10.00 per bushel) than to pay the shipping costs to the futures buyer in Chicago. The hedging function remains the same, however.

39 *Id.*

40 *Id.*

41 Futures Markets, *supra* note 19.

1. Background

In 2004, two information markets outperformed 99.5% of their competitors in a season-long contest to predict the outcomes of professional football games.[42] In 2005, another information market traded contracts in eight major Oscar categories and correctly predicted the winner of each.[43] Information markets have also outperformed political polls[44] and forecasts of the National Weather Service.[45]

These predictive successes have prompted various organizations to adopt information markets as predictive mechanisms. Hewlett-Packard employed an information market to predict printer sales and the market beat its experts fifteen out of sixteen times.[46] In 2003, the Department of Defense created a program called FutureMAP, attempting to use an information market to predict future terrorist attacks, but cancelled it after a barrage of critical press.[47] Some academics have advocated an even wider use for these predictive markets: Professor Robin Hanson, a designer of FutureMAP,[48] has advocated substituting information markets for academic journals, since information markets reward accuracy rather than popularity;[49] Professor Tom W. Bell has argued that information markets should be used as a complement to intellectual property laws to promote science and the useful arts;[50] and Professors Michael Abramowicz and Cass Sunstein have advocated using information markets to improve cost-benefit analysis[51] and group deliberation,[52] respectively.

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42 The markets finished 6th and 8th out of 1,947 competitors. Emile Servan-Schreiber et al., *Prediction Markets: Does Money Matter?* 14 ELECTRONIC MARKETS 1, 8 (2004).

43 Cass R. Sunstein, *Group Judgments: Statistical Means, Deliberation, and Information Markets*, 80 N.Y.U. L. REV. 962, 1031-32 (2005).

44 The Iowa Electronics Market has been more accurate than political polls in 75.6% of sample elections, or 451 out of 596. Hahn & Tetlock, *supra* note 1, at 266.

45 Richard Roll, *Orange Juice and Weather*, 74 AM. ECON. REV. 861, 871 (1984).

46 Hahn & Tetlock, *supra* note 1, at 266.

47 Abramowicz, *supra* note 5, at 933. For criticism of FutureMAP, see, for example, Pearlstein, *supra* note 5; Wyden & Dorgan, *supra* note 5.

48 Ronald Bailey, *Betting on Terror: Why Futures Markets in Terror and Assassinations Are a Good Idea*, Reason Online, July 30, 2003, http://www.reason.com/rb/rb073003.shtml (crediting Professor Hanson as a designer of FutureMAP).

49 Hanson, *supra* note 3, at 399, 401, 403-06.

50 Tom W. Bell, *Prediction Markets for Promoting the Progress of Science and the Useful Arts*, 14 GEO. MASON L. REV. 37 (2006).

51 Abramowicz, *supra* note 5, at 940.

52 Sunstein, *supra* note 43, at 969.

Several less scholarly information markets are already active and accessible on the internet.[53] These markets trade contracts on everything from political, financial and sporting events to box office revenues, using both real and play money.[54] Because these internet markets trade on a wide array of topics—including sports—some academics who support legal real-money markets consider such markets gambling.[55]

The predictive success of, and academic support for, information markets stem from their structure.[56] The simplest form of information markets,[57] also called prediction markets, artificial markets, event markets,[58] and idea futures,[59] operate as contract exchanges. The contracts allow market traders to place bets on the occurrence, or non-occurrence, of uncertain future events by taking the form of contingent assets.[60] Contingent assets can best be understood as "X if A," where X is the payoff and A is an uncertain future event.[61]

For example, if A owns a "$10.00 if it Rains on Monday" contract, she will unsurprisingly be entitled to $10.00 if it rains on Monday .[62] Conversely, B will be entitled to $0.00 for his "$10.00 if No Rain Monday" contract. These contracts are initially issued by the exchange by selling a pair of mutually exclusive contracts—such as those to A and B in the above example—for a sum equal to the payoff.[63] The exchange could issue A and B their rain contracts for $5.00 each, and thus the market's intake would be $10.00, the amount of the contract's payoff.[64] The issuer itself takes no risk in issuing the contract, because its receipts will always equal its payout

53 There are currently more than twenty-three online information markets. Hahn & Tetlock, *supra* note 1, at 266.

54 Sunstein, *supra* note 43, at 1033-34.

55 *See, e.g.*, Hahn & Tetlock, *supra* note 1, at 268.

56 *See id.* at 266.

57 More complicated forms of information markets, based on conditional rather than binary payoffs, are largely outside the scope of this paper, although they are fascinating in their own right. *See generally* Abramowicz, *supra* note 5, at 952-57.

58 Hahn & Tetlock, *supra* note 1, at 266.

59 Hanson, *supra* note 3, at 403.

60 *Id.* at 404-06.

61 *Id.* at 412.

62 This "Rain on Monday" example comes from Professor Robin Hanson's lucid description of information markets. *Id.* at 411-12.

63 *Id.*

64 The initial prices for A and B need not be equal. If meteorologists were predicting rain on Monday, it might require reducing the price of B's no rain contract to induce him to wager on it not raining.

whether it rains or not.[65] Once A and B have their contracts, they are free to trade them with others in a secondary market.[66]

The market's predictions stem from the prevailing price for these contracts set in the secondary market.[67] These prices reveal a prediction of an event's occurrence because they are the expected value of the contract.[68] The expected value of a contract is the total payoff times the percentage chance that the payoff event will occur. To illustrate, if A thought there was a 30% chance of rain on Monday, his "$10.00 if it Rains on Monday" contract would have an expected value of $3.00, which equals the percentage chance he will receive the payoff, 30%, multiplied by the contract payoff, $10.00.[69] It would be a losing proposition for A to buy a contract for more than $3.00 if he felt there was a 30% chance of rain, because he would be paying more than he expected the contract to be worth. Since all market participants should behave in this manner, the prevailing market price therefore reflects the aggregate percentage prediction of all market participants. If some market participants believed there was a 45% chance of rain, it would be profitable for those participants to purchase all contracts available below $4.50, and the price would then rise until it reached that point. The expected value can actually be the full contract price if there is an insider in the market that knows the outcome of the event, such as an expert meteorologist.[70] In sum, the price in the secondary market, when taken as a percentage of the contract's payoff, reveals the market's percentage prediction of an uncertain future event.[71]

Not only do the prices reflect the market's prediction, there are reasons to think such a prediction should be accurate: (1) almost anyone can participate by trading contracts; (2) superior information equates to profits; and (3) profits motivate people to look for superior information.[72] For example, profits would be available to any eligible trader who had information that the market was incorrectly predicting the chance of rain on Monday. These profits provide an incentive for all eligible traders to discover that information and purchase inaccurately priced contracts. Purchasing contracts funnels information into the market and moves the contract price to a more accurate percentage chance of rain on Monday. One study indicated that the presence of only a small number of insiders with knowledge

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65 Hanson, *supra* note 3, at 411.
66 *Id.*
67 *Id.*
68 *See* Charles R. Plott, *Markets as Information Gathering Tools*, 67 S. ECON. J. 1, 9-10 (2000).
69 Hanson, *supra* note 3, at 411-12.
70 Plott, *supra* note 68, at 9.
71 *See, e.g.*, Hahn & Tetlock, *supra* note 1, at 266; Servan-Schreiber et al., *supra* note 42, at 8.
72 Hahn & Tetlock, *supra* note 1, at 266.

of the true price is sufficient to bring the market price to the true price.[73] Although these markets may be susceptible to various forms of manipulation, Professor Robin Hanson evaluated the susceptibility of information markets to lying, manipulation, sabotage, embezzlement, and retribution and concluded that they are no more susceptible than other forecasting mechanisms.[74] The foregoing discussion explains information markets generally. Because this comment focuses on sports futures, however, an example of a sports futures market is also necessary.

2. Tradesports – A Specific Example[75]

One highly-publicized[76] online information market is Ireland-based Tradesports, a wholly owned-subsidiary of Trade Exchange Network.[77] Despite being based in Ireland, 33-40% of Tradesports customers are American.[78] As a result of locating in Ireland, though, Tradesports is not regulated by any authority.[79] Tradesports offers contracts on everything from the outcome of English Premier League Soccer and Major League Baseball Games to whether the GOP will retain control of the House in the 2006 midterm election.[80]

On Tradesports, all contracts for the outcome of uncertain events have two mutually exclusive payoffs, each of which is possessed by a different trader. [81] For example, when A holds a "Redskins Win Sunday" contract,

73 Plott, *supra* note 68, at 9.

74 *Foul Play*, *supra* note 16, at 137-38.

75 Throughout this comment Tradesports and sports futures will be used interchangeably. Thus, whenever sports futures are mentioned, it can be assumed they will be traded in the format used on Tradesports, and when Tradesports is mentioned, it refers only to their sports futures.

76 Tradesports has been the subject of articles in Fortune and the New York Times, among others. Media Coverage of Tradesports, http://www.tradesports.com/press (last visited Sept. 10, 2006). *See, e.g.*, Andy Serwer, *Making a Market in (Almost) Anything*, FORTUNE, Aug. 8, 2005, at 103, 104-06; Hal R. Varian, *A Market Approach to Politics*, N.Y. TIMES, May 8, 2003, at C2.

77 About Tradesports, http://www.tradesports.com/aav2/aboutUs.jsp (last visited Sept. 10, 2006).

78 Press Release, CFTC, *supra* note 11. This is lower than one estimate of the percentage of total online wagering by Americans, which places Americans as the source of about 80% of all dollars wagered online. *60 Minutes*, *supra* note 10.

79 Trade Exchange Network, C.F.T.C No. 05-14 (Sept. 29, 2005), 2005 C.F.T.C. LEXIS 100, at *3 [hereinafter Trade Exchange Network]. The CFTC instituted an administrative proceeding against Trade Exchange Network for "actively solicit[ing] U.S. residents" to trade outlawed commodity option contracts in 2005, but Trade Exchange Network voluntarily offered a settlement offer to CFTC, leaving the question of jurisdiction unresolved. *Id.* at 4.

80 *See* Tradesports' Most Active Today, http://www.tradesports.com/aav2/trading/tradingHTML.jsp (last visited Sept. 10, 2006).

81 Tradesports Frequently Asked Questions on Trading, http://www.tradesports.com/aav2/rulesAn

another trader holds a "Redskins Lose Sunday" contract. Regardless of who wins the game, only one of the two traders will receive the payoff.[82]

Prices on Tradesports are listed 0.00-100.00.[83] These prices do not denominate currency,[84] but instead represent a percentage of the contract's full price, such that a $10.00 contract trading at 20.00 would cost $2.00 to buy.[85] Thus, a $10.00 "Redskins Win" contract at 100.00 would be worth $10.00, and at 0.00 would be worth $0.00. These prices display the percentage-chance the market is giving the contract of paying off.[86] For example, a contract trading at 20.00—20% of the contract's value (100.00) if its payoff event occurs— indicates that there is a 20% chance that contract will pay off.[87] It is also this purchase price that determines each trader's potential profit or loss from the contract.[88] If A bought a $10.00 contract on the Yankees in that day's baseball game at a market price of 10.00, or $1.00, then upon the Yankees victory, the contract price would become 100.00 and A would receive $10.00 in the contract payoff, leaving him with a profit of $9.00.[89]

Tradesports facilitates trades among its customers by matching all the purchase offers with sell offers at the same price.[90] For example, if A wanted to purchase a contract at 10.00 on the Yankees winning that day's baseball game, Tradesports would match A's offer to purchase at 10.00 with B who was willing to sell at 10.00.[91] Tradesports calls this type of contract, in which A takes the prevailing market price, a price-taker contract.[92]

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dFaqs.jsp?helpPage=trading (last visited Sept. 10, 2006) [hereinafter Tradesports Trading]. Recall the mutually exclusive payoffs of A and B's "Rain on Monday" contracts: A received the payoff if it rained, and B received the payoff if it did not, but in no case would both have received the payoff. Hanson, *supra* note 3, at 411-12.

82 When the outcome of the event occurs, the holder of the winning contract receives the full contract price and the holder of the other mutually exclusive alternative receives nothing.

83 Tradesports Trading, *supra* note 81 ("Zero to One Hundred (0-100) pricing is used for the majority of contracts on the Exchange. Prices are quoted 0-100, which is in effect a percentile representation of the likelihood of a specific outcome or the probability of something actually happening.").

84 *Id.* Therefore, a price of 20.00 does not indicate that the contract costs $20.00 to purchase.

85 *Id.*

86 *Id.*

87 *Id. See supra* notes 67-71 and accompanying text for a more detailed explanation of how the market price shows the likelihood of an event occurring.

88 Tradesports Trading, *supra* note 81.

89 *Id.* This can most easily be understood by realizing that A invested $1.00 to win $10.00 (he paid the 10.00 market price to win the 100.00 price of a winning contract), leaving him with $9.00. Similarly, B invested $9.00 to win $10.00, and since his contract expired with a value of 0.00, he lost his $9.00. The total amount invested by A and B is equal to the contract price. *Id.*

90 *Id.*

91 *Id.* Note again that by B selling the contract at 10.00, he is essentially buying the contract on the Yankees loss for 90.00, or investing $9.00 to win $10.00.

92 Tradesports' Rates and Fees, http://www.tradesports.com/aav2/rulesAndFaqs.jsp?helpPage=ru

If there was no other trader willing to sell that contract at 10.00 at that time, Tradesports would hold A's purchase order until a trader willing to sell that contract appeared or the contract expired.[93] This situation, in which a trader seeks to create their own price rather than execute a trade at the market price, is called a price-maker contract.[94]

Tradesports itself never purchases or sells a contract on the market.[95] The exchange charges a flat fee of $0.04 for each $10.00 Price-Taking contract bought or sold, and also the same fee for each contract when the contract expires.[96] This amounts to a total fee of $0.16 for every $10.00 traded, or 1.60%. The preceding descriptions of information markets and Tradesports reveal at least superficial similarities between sports futures and both gambling and investing. The next part evaluates sports futures' similarities to each activity under the gambling-investing dichotomy.

II. THE FUTILITY OF DIFFERENTIATING BETWEEN GAMBLING AND INVESTING

The United States government distinguishes between activities it considers gambling and those it considers investing. Such a formalistic policy, despite receiving valid criticism, has persevered for more than a century. This part explains and rejects the purported rationale for this policy, and offers an explanation for the policy's perseverance. It concludes by rejecting an explanation for the particularly harsh way the government applies the policy to online gambling.

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les&rules=rates-fees (last visited Sept. 10, 2006) [hereinafter Tradesports' Rates and Fees].

93 *See id.*

94 *Id.* Tradesports does not charge commissions on price-maker contracts. *Id.*

95 Tradesports' Most Asked Questions, http://www.tradesports.com/aav2/rulesAndFaqs.jsp?helpPage=mostAsked#10 (last visited Sept. 10, 2006).

96 Tradesports' Rates and Fees, *supra* note 92. A brief explanation of the concept of contracts lots is necessary to understand Tradesports' fee structure. One lot is worth up to $10 traded on each contract. *Id.* So to trade $40 in one contract, the trader would be trading 4 lots of that contract. *Id.* Tradesports charges each party to contract $0.04 per lot traded at the time of the transaction, and again when that contract closes, making the total cost $0.16 per $10.00 traded, or 1.6%. *Id.* In the event your transaction is not processed immediately—called a price-maker contract—you will not be charged a transaction fee, but will still be charged a closing fee. *Id.*

A. *Testing Sports Futures Against the Rationale for Prohibiting Gambling*

Gambling has been illegal in the United States for the last 100 years, with but a few exceptions.[97] Prior to that, gambling was fairly widespread and included betting on races, cards, and particularly lotteries, which many private institutions used to raise capital.[98] State governments used lotteries as a form of bond offering, with states allowing private businesses to run the lottery and then take some portion of the proceeds.[99] Lotteries paid for the Nation's troops in the Revolutionary War, and to improve the Erie Canal.[100] These private lotteries were eventually offered solely for private purposes, and some were found to be fraudulent.[101] By 1894, all states had outlawed lotteries and many other forms of gambling.[102] However, since 1964, forty states and the District of Columbia have legalized and conduct state-run lotteries.[103] In addition, many states have legalized pari-mutuel horse and dog-racing,[104] and gambling of some type is legal in "every state but two."[105] Those two states are Utah and Hawaii.[106]

The liberalization of gambling policy since 1964 has not reached sports betting. Nevada is currently the only state with a thriving legal sports betting industry.[107] Sports betting has been singled out as particularly destructive because the telephone allows bettors to wager without having to travel to the bookie.[108] This unique feature of sports betting prompted the federal government to enact The Wire Act in 1961.[109] Furthermore, sports gambling has a wider appeal than horse or dog-racing because the mainstream sports have a much larger following. A study performed by the National Gambling Impact Study Commission estimated that sports gambling was a $380 billion industry in the United States.[110]

97 Hurt, *supra* note 8, at 374 .
98 *Id.* at 394-97.
99 *Id.* at 394-95.
100 *Id*. at 394.
101 *Id*. at 395.
102 *Id.* at 395-96.
103 Hurt, *supra* note 8, at 398.
104 *Id.* at 398-99.
105 *60 Minutes*, *supra* note 10.
106 Jonathan Gottfried, *The Federal Framework for Internet Gambling*, 10 RICH. J.L. & TECH. 26, ¶ 5 (2004), http://law.richmond.edu/jolt/v10i3/article26.pdf.
107 Hurt, *supra* note 8, at 399-400.
108 *Id.*
109 *Id.*
110 *Id.* at 400; Levitt, *supra* note 32, at 223.

An explanation of traditional sports books is useful in comparing Tradesports to other sports gambling. Bookies accept bets from clients, and thereby expose themselves to betting losses. To make a profit, they force bettors to risk more than they stand to gain on each bet. This additional amount is called the "juice," "vig," or vigorish," and can be as much as 10%.[111] For example, a bettor would be required to pay $110 if his bet lost, but would only receive $100 if it won.[112] The "juice" is critical to a bookie's success because it ensures the bookie will make a profit if there is equal money on each side of the contest.[113] For example, if $500 is bet on each team in a football game, the losing bettors will pay the bookie $550, and the bookie will pay the winning bettors only $500, leaving him a profit of $50.

In order to encourage even money on both sides, bookies handicap the favorite with "the line."[114] The line is a number of points over which the favorite must outscore the underdog for bets on the favorite to win.[115] Therefore, a bet on the "Redskins minus four" would require the Redskins to outscore their opponent by more than four points for a bet on the Redskins to pay off.[116] As the bets come in, the bookie will shift the line to encourage betting on the out-of-favor team and re-attain equilibrium.[117] If the line is placed correctly, the money will be evenly divided and the bookie will simply pocket the "juice."[118]

Notwithstanding the bookies' best efforts to minimize their exposure,[119] they do have significant exposure if the line is not set to keep the wagers evenly split.[120] One example was an event called "Dettori Day."[121] A

111 ARTHUR S. REBER, THE NEW GAMBLER'S BIBLE 278 (1996); Levitt, *supra* note 32, at 224.

112 REBER, *supra* note 111, at 278; Levitt, *supra* note 32, at 224 n.3.

113 REBER, *supra* note 111, at 276; Levitt, *supra* note 32, at 224.

114 REBER, *supra* note 111, at 276.

115 *Id.* at 277.

116 *Id.*

117 *Id.* at 276.

118 *Id.*; Levitt, *supra* note 32, at 224 n.4.

119 The operation in the text represents the traditional view of sports books, but economist Steven D. Levitt conducted a study of one online bookie and concluded that sports books do not actually attempt to set the line to balance wagers on both sides of the event. Levitt, *supra* note 32, at 225. Instead, bookies attempt to place the line at a point which will capitalize on bettor preferences for visiting teams and favorites. *Id.* Bookies therefore "set odds such that favorites and home teams win less than 50% of the time, yet attract more than half of the betting action." *Id.* at 226. As evidence of this strategy, Levitt found that in one-half of football games, more than two-thirds of the wagers were on one team, and that by manipulating the line in this manner, bookies can increase their profits by twenty to thirty percent. *Id.* Even if Levitt's observations are correct, however, the analysis of this section remains unchanged since moving the line in this way only makes bookies' exposure intentional rather than inadvertent.

120 *See id.* at 223-24 ("If that [line] is not the market clearing price, then the bookmakers may be exposed to substantial risk.").

British jockey, Frankie Dettori, rode the winner in all seven horse races on September 28, 1996.[122] Because they were prominent races, so highly wagered, and so much of the total wagers occurred off track, the odds at the track were not able to adequately adjust, and bookies throughout Great Britain lost an estimated £40 million on that day alone.[123]

There are two major reasons why gambling is so maligned in the United States. First, critics argue that gambling causes social ills such as addiction, bankruptcy, crime and welfare.[124] Medical evidence supports gambling's connection to addiction. The American Psychiatric Association identifies pathological gambling in the Diagnostic and Statistical Manual of Mental Disorders IV ("DSM-IV") as an "impulse control disorder."[125] Social or professional gambling becomes pathological gambling when gambling develops into a persistent and maladaptive pattern that causes difficulties with interpersonal, financial and vocational activities.[126] Symptoms of pathological gambling include preoccupation with gambling, irritability when attempting to stop, unsuccessful attempts to stop, gambling as a means of escape, and an increase in gambling to recover previous losses.[127] Additionally, studies in the United States and Australia show that approximately 1% of the adult population has severe or pathological gambling problems.[128] In the United States, that 1% of the adult population represents 6% of the gambling industry and accounts for 15% of all money gambled.[129] Some have estimated $5 billion in other gambling-related social costs, including crime, welfare, and bankruptcy.[130] However, none of the studies that show an increase in bankruptcy and crime following the introduction of casinos to an area establish an exact causal link between the two.[131]

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121 This example occurred under a betting structure slightly different from that described in the text. Horse racing bookies alter the odds (i.e., the amount of "juice") on each horse rather than handicapping the horses per se, but "Dettori Day" is nonetheless a perfect example of bookies' exposure to gambling losses that are caused by human error. JOHN HAIGH, TAKING CHANCES 227 (2003).

122 Id.

123 *Id.*

124 Hurt, *supra* note 8, at 402.

125 AM. PSYCHIATRIC ASS'N, DIAGNOSTIC AND STATISTICAL MANUAL OF MENTAL DISORDERS § 312.31 (4th ed. 2000) [hereinafter DSM-IV].

126 *Id.*

127 *Id.*

128 Gottfried, *supra* note 106, ¶ 27.

129 *Id.* ¶ 28.

130 John Andrle, Comment, *A Winning Hand: A Proposal for an International Regulatory Schema with Respect to the Growing Online Gambling Dilemma in the U.S.*, 37 VAND. J. TRANSNAT'L L. 1389, 1392 (2004).

131 Hurt, *supra* note 8, at 426.

Second, gambling is maligned because many believe—and have believed since the nineteenth century—that gambling violates the Puritan work ethic.[132] Protestant ministers preached that profit without work was immoral, including profits from stock trading.[133] This position marked a change from past doctrine because all Christian denominations—save the Quakers—operated lotteries prior to the turn of the century. [134] Nonetheless, the criticism stuck, and it was largely responsible for the disappearance of legalized gambling in the late-nineteenth and early-twentieth century.[135] That opprobrious view of gambling also fuels modern attempts at prohibition. For example, following the House's passage of the Internet Gambling Prohibition and Enforcement Act ("IGPEA") on July 12, 2006, Majority Leader John Boehner hailed the bill as "substantive legislation upholding strong values that puts the interests of our families and children first."[136] Opponents of gambling also still argue that it encourages sloth by allowing people to earn wealth without doing any work.[137]

In addition to the two foregoing criticisms leveled against sports books and gambling generally, opponents frequently claim that online gambling creates four additional social ills: fraud, money-laundering, addiction, and underage gambling.[138] First, fraud is a concern with online gambling because the games are played using an algorithm to simulate random chance, rather than the actual chance associated with cards or dice.[139] Opponents to online gambling are concerned that online casinos could alter the odds against participants while representing that they are similar to regular casinos.[140] Additionally, there is a concern that online casinos may disappear with customer funds or refuse to pay when obligated.[141] Senator Jon Kyl (R-AZ), who wrote a bill prohibiting domestic banks and credit card companies from conducting any online gambling transactions, notes that because most online gambling "is done in foreign countries. . . . even if [Congress

132 *Id.* at 396.

133 *Id.* at 377 n.28.

134 *Id.* at 395 n.142 (citing JOHN LYMAN MASON & MICHAEL NELSON, GOVERNING GAMBLING 8 (2001)).

135 *See id.* at 396.

136 Press Release, Representative John Boehner, Boehner: House Passes 2nd American Values Agenda Bill, Cracks Down on Internet Gambling (July 11, 2006), *available at* http://johnboehner.house.gov/news.asp?FormMode=Detail&ID=1192.

137 Hurt, *supra* note 8, at 373 n.10 (citing JOHN GILMORE, LOTTO: FUN OR FOLLY 28-30 (2001)).

138 Gottfried, *supra* note 106, ¶ 14.

139 Hurt, *supra* note 8, at 428.

140 *See* Gottfried, *supra* note 106, ¶ 16.

141 Id.

tries] to create some kind of standards, it's not to say that it's going to be enforced by a foreign government."[142]

Second, online gambling might facilitate money-laundering, the process of funneling illegally generated money through a legitimate operation to hide its illegitimate source.[143] The routine nature of large cash transactions in gambling allows criminals to quickly funnel illegally-begotten money through a legitimate business.[144] Opponents argue that a criminal operation could make large cash deposits at an online casino and then make a few modest wagers and withdraw the money as legitimate casino winnings.[145]

Third, online gamblers are believed to be more prone to gambling addiction. The ability of problem gamblers to gamble twenty-four hours a day provides a greater potential for a gambling addiction.[146] Critics also argue that online gamblers can more easily hide their addiction and therefore may not receive help from friends and family.[147] Additionally, unlike in brick-and-mortar casinos, there are no tangible assets like in online casinos to remind gamblers how much they have lost.[148] Senator Kyl also notes there is little chance of "some outfit in Aruba" knocking on a customer's door and telling him he is gambling too much.[149]

Finally, the internet is believed to provide a better opportunity for adolescents to gamble. The lack of physical identification on the internet makes it plausible that children would be able to gamble in online casinos.[150] Also worrisome is that even if minors do not actually gamble online, they may become exposed to and enthralled by gambling and develop gambling problems later in life.[151]

The foregoing rationale for prohibiting gambling applies to sports futures. Although the form of those contracts is not that of a traditional bet, it clearly enables money to be risked on the outcome of a sporting event, an activity the federal government views with disapproval. Furthermore, traders can use the internet to trade on the exchange from anywhere in the world, giving sports futures the same long-distance potential that led to the passage of The Wire Act. Such an activity could lead to addiction, as well as crime, welfare, and bankruptcy if traders lose all their money.

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142 *60 Minutes*, *supra* note 10 (interviewing Senator Jon Kyl).
143 Gottfried, *supra* note 106, ¶¶ 19-20.
144 *See id.* ¶ 20.
145 *Id.*
146 *Id.* ¶ 28.
147 Hurt, *supra* note 8, at 418.
148 Gottfried, *supra* note 106, ¶ 28.
149 *60 Minutes*, *supra* note 10 (interviewing Senator Jon Kyl).
150 *See* Gottfried, *supra* note 106, ¶ 33.
151 *See id.* ¶ 36.

Additionally, all of the arguments raised against online gambling apply to Tradesports. Tradesports is not regulated.[152] Therefore, it would be possible for fraud and money-laundering to occur on its exchange. Furthermore, Tradesports allows people to trade at home without social restraints, and does not verify the age of those who trade on their exchange. Tradesports allows trading twenty-three hours per day; its exchange closes for one hour each day to update accounts and undertake maintenance.[153] Thus, Tradesports exhibits the negative aspects of gambling in general, as well as those specific to sports gambling and online gambling.

B. *Testing Sports Futures Against the Rationale for Regulating Investing*

The previous section concluded that sports futures satisfy traditional conceptions of gambling. If gambling and investing are actually distinct activities, then no activity could correctly be classified as both gambling and investing. The existence of an activity with a dual-classification demonstrates that the two are not fundamentally distinct, and therefore the premise of the dichotomy is untenable. This subpart tests the trading of sports futures against traditional investing rationales to determine if it is such a dually-classified activity.

The government has chosen to regulate rather than prohibit investing. Investment markets serve socially beneficial purposes and are regulated rather than prohibited to allow fulfillment of these functions. For example, debt and equity markets provide financing for corporations that need it, and futures markets allow for hedging and price discovery and dissemination.[154] Modern portfolio theory provides additional reasons for allowing investing devices.[155] Simply put, modern portfolio theory teaches that by diversifying the assets in any portfolio, investors can reduce the variance in their returns.[156] Accordingly, market regulators encourage the development of new financial instruments in order to provide greater diversification of investment opportunities.[157] Diversification can reduce risk whenever there is "anything less than perfect positive correlation" of assets in a portfolio.[158]

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152 Trade Exchange Network, *supra* note 79, at *3.

153 Tradesports' Exchange Hours, http://www.tradesports.com/aav2/rulesAndFaqs.jsp?helpPage=rules&rules=exchange-hours (last visited Sept. 10, 2006).

154 Futures Markets, *supra* note 19.

155 *See generally* BURTON G. MALKIEL, A RANDOM WALK DOWN WALL STREET 206-19 (rev. ed., W.W. Norton & Co. 1999) (1973) (discussing modern portfolio theory).

156 See id. at 206.

157 *See* Hazen, *supra* note 31, at 994-95, 1021.

158 MALKIEL, *supra* note 155, at 211. An idealized illustration of this effect is an island man owning an umbrella store and also owning a sunscreen store. In the event of rain, he sells $50.00 of umbrel-

Diversifying stocks with other stocks can be difficult, however, because the "fortunes of most companies move pretty much in tandem."[159] Thus, in an effort to find assets that do not move in tandem, many portfolio managers seek out international stocks,[160] or mix real estate,[161] bonds,[162] and commodities[163] with domestic stock portfolios. Seeking to diversify into international stocks can be difficult for smaller investors because some overseas markets restrict the amount of "foreign ownership with smaller levels of investment."[164] Financial derivatives could be used to circumvent these restrictions, because the derivative would be correlated with the international security but does not require ownership of that security, and thus does not trigger foreign ownership restrictions.[165]

Indeed, the primary justification for derivatives like futures contracts is that they reduce risk.[166] Futures contracts allow holders of the underlying asset the ability to hedge against price fluctuation in that asset.[167] Prior to the CFTC's creation, futures contracts could only be used to hedge risk because speculation on futures contracts was illegal.[168] Currently, the CFTC acknowledges the prevalence and benefit of speculation in futures markets.[169] Speculation occurs whenever someone trades in futures with no intention of ever delivering or receiving the underlying asset.[170] Today, as long as a future contract is traded on an authorized exchange, the trade is legal regardless of any lack of intention to deliver or accept the underlying asset.[171] And indeed, over 90% of futures contracts currently traded are

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las, and no sunscreen. But in the event of a sunny day, he sells $50.00 in sunscreen and no umbrellas. Thus, by owning both businesses the islander has completely removed any variation in his daily sales since he sells $50.00 of something everyday. *Id.* at 207-08.

159 *Id.* at 209.

160 *Id.* at 212 ("[Investors] can reap even greater protection because the movement of foreign economies is not always synchronous with that of the U.S. economy.").

161 *Id.* at 218 ("Real estate returns don't always move in lockstep with other assets. . . . Thus, adding real estate to a portfolio tends to reduce its overall volatility.").

162 *Id.* at 219 ("Movements in long-term bonds do not mirror those of other assets, and long-term bonds tend to provide relatively stable returns when held to maturity.").

163 *Id.* at 286 ("[G]old . . . art objects, commodities, and other more exotic investment possibilities . . . have done very well, especially when inflation was accelerating, and can serve a useful role in balancing a well-diversified portfolio of paper assets.").

164 Mark Gillen & Pittman Potter, *The Convergence of Securities Laws and Implications for Developing Securities Markets*, 24 N.C. J. INT'L L. & COM. REG. 83, 107 (1998).

165 *Id.*

166 Futures Markets, *supra* note 19.

167 See supra Part I.A.

168 *See* Hazen, *supra* note 31, at 1016-17.

169 Speculators add liquidity to the market and increase its efficiency in price discovery and hedging. Futures Markets, *supra* note 19.

170 Hazen, *supra* note 31, at 1015-16.

171 *Id.* at 1016-17.

closed by purchasing an offsetting contract rather than delivering the asset.[172]

While these positive features explain why investing activities are regulated rather than prohibited, the idea that markets are rational and efficient dictates how they are regulated.[173] Efficient markets adequately incorporate and reflect all information in the prevailing market prices.[174] The market's intrinsic ability to incorporate all information leads proponents of the rational markets theory to believe there is not a need for stringent market regulations:[175] when an investor realizes there is misinformation in the market, he will purchase or sell securities until that information is no longer factored into the market.[176] This means misinformation is problematic only if no trader identifies it as misinformation.[177] It follows that the more traders there are in a market, the more efficient it becomes because there are more traders to identify misinformation.[178] This positive correlation between the number of traders and a market's efficiency leads the government to encourage more participation by adopting a laissez-faire regulatory structure.[179]

The efficient markets hypothesis does not mean that absolutely no regulation is needed. Releasing incorrect information will still mislead the market so long as nobody else can identify it as misinformation.[180] Such manipulation would be possible if companies falsified corporate information to which no one else had access. In response, the government has long enforced corporate disclosure requirements to prevent the release of corporate misinformation.[181] The belief that markets reflect all available information is also embodied in the fraud-on-the-market presumption in securities litigation.[182] Fraud-on-the-market assumes that any misrepresentation by a publicly-traded company has distorted the stock price, damaging the plaintiff, and plaintiffs are only required to show that a misrepresentation occurred.[183] Also in accordance with the efficient markets hypothesis, the

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172 *Id.* at 1017.
173 *Id.* at 994.
174 *Id.* at 995; Plott, *supra* note 68, at 12-13.
175 Hazen, *supra* note 31, at 993-94.
176 *See* Plott, *supra* note 68, at 9-12.
177 *See id.*
178 *See id.*
179 *See* Hazen, *supra* note 31, at 991-92, 1012-13.
180 *See* Plott, *supra* note 68, at 9-12.
181 Hazen, *supra* note 31, at 1014.
182 *Id.* at 995.
183 *Id.*

CFTC regulates futures markets mostly by ensuring against market manipulation.[184]

The foregoing rationale for allowing and regulating investing applies to sports futures. Trading sports futures can diversify a portfolio of other assets, and is therefore valuable under modern portfolio theory. Since outcomes of sporting events are non-economic events, they should actually yield a far greater reduction in variance than would adding additional economic assets to an investment portfolio. Furthermore, derivatives have been used to capture the diversification benefits of foreign securities whose direct ownership would violate the law.[185] It should not be problematic that sports futures allow people to do indirectly what they cannot do directly. Nor should it be problematic even if very few sports futures are traded with the intention of diversifying a portfolio since more than 90% of all other futures contracts are traded for purely speculative purposes.[186] Just as the CFTC acknowledges that efficiency is improved by the presence of speculators,[187] it should also acknowledge the presence of speculators in the sports futures market will make that market more efficient.

This subpart and the preceding one have shown that sports futures are both investing and gambling. This is a damning finding—and maybe the deathblow—for a policy that purports to draw a categorical distinction between the two. If the dichotomy predicated upon distinguishing gambling and investing cannot do so, then its disparate treatment of the two must be based upon something less principled and more arbitrary. The next subpart explains why the dichotomy is incapable of drawing a coherent distinction between the two.

C. *Debunking the Gambling-Investing Dichotomy*

The preceding two subparts showed that the gambling-investing dichotomy fails because the two activities are so similar that distinguishing between them cannot be accomplished in a principled manner.[188] This subpart demonstrates the intrinsic similarities of the two activities by examining several unsuccessful attempts to narrowly define gambling without including investing. It also demonstrates that the two activities cannot be dis-

184 *Id.* at 1016-17.

185 Gillen & Potter, *supra* note 164, at 107.

186 *See* Hazen, *supra* note 31, at 1017.

187 *See* Futures Markets, *supra* note 19.

188 This point has also been made by Professor Christine Hurt. Hurt, *supra* note 8, at 377 ("Any attempt to substantively distinguish all types of gambling (from slot machines to poker to sports betting) from all types of investing (from long-term ownership to day trading to purchasing derivatives) is illusory.").

tinguished based on their respective consequences, because every negative consequence of gambling is also a consequence of some investing activities.

Although everyone understands what gambling is, a definition of gambling narrow enough to exclude investing activities is likely impossible to formulate.[189] A narrow definition is so difficult that "one of the finest research tools produced in the twentieth century,"[190] the scholar's edition of the Encyclopædia Britannica, was forced to admit that "[i]t is somewhat difficult exactly to define" gaming or wagering.[191] Statutory definitions are illustrative of this problem. Florida's statutory definition begins by listing several common gambling activities like playing cards, keno or roulette, and then concludes with the broad catch-all, "or other game of chance, at any place . . . for money or other thing of value."[192] Wyoming also defines gambling in extremely broad terms: "'Gambling' means risking any property for gain contingent in whole or part upon lot, chance . . . or the happening or outcome of an event . . . over which the person taking a risk has no control."[193] A definition as broad as Wyoming's is problematic because it includes regulated investing activities like stock trading. In fact, Wyoming's definition is so broad, the drafters felt it necessary to carve out exceptions for "bona fide business transactions which are valid under the law of contracts" and "[o]ther acts or transactions . . . authorized by law . . . ."[194] Federal lawmakers have been no more successful, as the IGPEA failed to define gambling so as to exclude investing activities.[195] To ensure the statute did not criminalize investing activities, the House of Representatives included an exception for "any activity governed by securities law . . . for the purchase or sale of securities" or other activities valid under or exempt from the Commodities Exchange Act.[196]

Scholars have defined gambling as "taking an initial risk for the possibility of eventual gain"[197] and "economic choices under uncertainty."[198]

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189 R. Randall Bridwell & Frank L. Quinn, *From Mad Joy to Misfortune: The Merger of Law and Politics in the World of Gambling*, 72 MISS. L. J. 565, 616 (2002).

190 *Id.* at 617 n.177.

191 *Id.* at 616 (citing HUGH CHISHOLM, ENCYCLOPÆDIA BRITANNICA 446 (11th ed. 1910)) (referring to the eleventh edition as the "definitive edition.").

192 FLA. STAT. ANN. § 849.08 (West 2000).

193 WYO. STAT. ANN. § 6-7-101(a)(iii) (2005).

194 § 6-7-101(a)(iii)(B)-(C).

195 Internet Gambling Prohibition and Enforcement Act, H.R. 4411, 109th Cong. (as placed on Senate calendar, July 13, 2006).

196 *Id.* § 101(3).

197 REBER, *supra* note 111, at 11.

Gambling so defined clearly incorporates traditionally illegal activities such as casino games, poker, pari-mutuel horse racing, and sports betting, but also includes traditionally legal investing activities like starting a business and buying stock.[199] Conversely, economist Burton Malkiel once described investing as "a gamble whose success depends on an ability to predict the future."[200] Notwithstanding these sentiments that investing and gambling are similar, the government has always regulated the two very differently without offering any persuasive justification.[201]

As discussed in Part II.A, gambling has been blamed for creating many social ills like addiction, crime, welfare and bankruptcy. Opponents of gambling paternalistically argue that gambling needs to be prohibited to prevent gamblers from exacerbating these social ills.[202] Insofar as gambling actually exacerbates such social ills, this is could be a valid reason to prohibit gambling. The problem is that investing activities can cause these social ills as well. Therefore, those consequences cannot be used to justify different treatment of the two activities.

As explained above, addiction is an "impulse control" problem. Accordingly, the problem is the addict's reaction to the gambling. Such a problem could be caused by any activity evoking such a reaction in the addict, regardless of whether it is labeled gambling or investing.[203] The DSM-IV itself lists playing the stock market as a gambling activity that can give rise to pathological gambling.[204] Additionally, the Connecticut Council on Problem Gambling acknowledges the potential of gambling addiction to surface in investors and published an online quiz to help traders identify the problem and seek help.[205] All medical support aside, a connection between investing and pathological gambling is intuitive since investing and gambling each involve placing something at risk for a potential future gain.

The other three social ills feared to spring out of gambling—crime, welfare, and bankruptcy—bear a similar relationship to investing. The link between these three ills and gambling is the fear that members of society will lose all of their money and resort to crime, welfare, and bankruptcy.

198 Hurt, *supra* note 8, at 373 (citing Antonio M.R. Vernón, Market Efficiency and March Madness: Empirical Tests of Point Spread Betting 1 (Dec. 23, 2003) (unpublished working paper, *available at* http://ssrn.com/abstract=340820)).

199 REBER, *supra* note 111, at 11.

200 MALKIEL, *supra* note 155, at 28.

201 *See* Hurt, *supra* note 8, at 374-77.

202 *See id.* at 402.

203 *See id.* at 404.

204 DSM-IV, *supra* note 125, at § 312.31 ("There are cultural variations in the prevalence and type of gambling activities (e.g., pai go, cockfights, horse racing, the stock market).").

205 Connecticut Council on Problem Gambling: Investing and Gambling Problems, http://www.ccpg.org/financial/investing_gambling_problems.asp (last visited Sept. 10, 2006).

While it is undoubtedly true that gamblers can squander all of their personal wealth and resort to crime, welfare, and bankruptcy, so too can investors. Popular culture abounds with stories of day traders suffering repeated losses,[206] and one study by the North American Securities Administration Association found that 70% of day traders lost money in the 1999 bear market.[207] Another study at a day trading firm revealed that sixty-seven out of the firm's sixty-eight day traders lost money. [208] Arthur Levitt, former chairman of the Securities Exchange Commission, once declared that day trading itself was not speculation "because traditional speculation requires some market knowledge. [Day traders] are instead gambling, which does not require market knowledge."[209]

A related criticism states gambling is an enterprise which systematically bilks working people out of their wealth by encouraging them to enter into negative-expectation bets.[210] If this were unique to gambling, it would make gambling more likely to cause crime, welfare and bankruptcy. It cannot be denied that gambling activities are negative-sum games: the actual odds at all casinos games like slots, blackjack, keno, roulette, and craps favor the house;[211] in games where the odds are even bookies force bettors to pay some amount of juice; and casinos take a "rake" in poker games.[212] Indeed, sports futures are no different. They are simply wealth-transfer contracts that are negative-sum when commissions are taken into account.[213] However, this is no different than any other derivative contract, which transfers one party's wealth to another, less the brokerage commission.[214] Therefore, it cannot be sufficient that an activity leaves the parties collectively in worse financial condition. If that alone were enough, all derivatives would need to be outlawed.

The criticism that gambling is immoral because it violates the Puritan work ethic appears to apply to gambling but not to investing. However, investing activities are in some cases more capable of providing unearned wealth than gambling activities, and therefore more offensive to the Puritan work ethic. The average stock investor knows very little about the prospective earnings of any company in which he is investing, but could benefit

206 *See* Hurt, *supra* note 8, at 404-05.

207 Meir Statman, Lottery Traders 9 (July 29, 2003) (unpublished working paper, *available at* http://ssrn.com/abstract=277158).

208 Arthur Levitt, *Plain Talk About On-Line Investing*, 51 ADMIN. L. REV. 1093, 1096 (1999).

209 *Id.*

210 *See* Hurt, *supra* note 8, at 373-74.

211 *Id.* at 380, 382.

212 A "rake" is a percentage of each pot taken by the house for managing the game, usually 10%. REBER, *supra* note 111, at 156.

213 *See supra* Part I.A for an explanation of negative-sum activities.

214 *See supra* Part I.A.

from a rising market despite his ignorance.[215] Indeed, most actively-managed mutual funds fail to beat the S&P 500,[216] leading many to recommend against actively trying to outguess the market or investing in funds that do.[217] This passive investment strategy can be quite lucrative: a one-time investment of $10,000 in the S&P 500 in 1969 increased thirty-one fold to $311,000 by 1998, yielding an average annual return greater than the initial investment.[218] In contrast, a successful sports gambler must be very skilled to consistently beat a sports book,[219] and a poker player skilled to consistently beat the "rake" at a casino.[220] It seems, therefore, that there are situations when stock investing is actually more offensive to the Puritan work ethic than either poker or sports betting. As a general response to the moral criticism, it is hard to believe something that is legal "in every state but two"[221] is immoral.[222]

D. *Why Has the Gambling-Investing Dichotomy Persisted?*

Professor Christine Hurt has advanced two theories for the motivation behind originally bifurcating gambling and investing: classist elitism and the self-interested action of the finance industry.[223] This subpart argues that while those two motivations may have led to the dichotomy's creation, its persistence is attributable mainly to an uncritical acceptance of the policy by succeeding generations of Americans. It must have been accepted uncritically, or the finance industry and the wealthy would have realized that their interests are better served by gambling's legalization.

The central argument against gambling at the turn of the twentieth century was that gambling was morally wrong and violated the Puritan work ethic.[224] Hurt posits that at least part of the rationale behind such rhetoric was an attempt by the wealthy to preserve social order.[225] There was a fear that the toss of the dice could make "a commoner a wealthy citi-

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215 Hazen, *supra* note 31, at 1006.

216 The S&P 500 is a stock index comprised of 500 large, public, American corporations. It is generally the benchmark against which mutual funds investing in large American companies are compared. *See* StreetAuthority.com, S&P 500 Index, http://www.streetauthority.com/terms/index/sp500.asp.

217 MALKIEL, *supra* note 155, at 13.

218 *Id.*

219 REBER, *supra* note 111, at 274 (stating that "while it is possible to beat your bookie, doing so is a tough proposition.").

220 *See id.* at 151.

221 *60 Minutes*, *supra* note 10.

222 *See* Hurt, *supra* note 8, at 402.

223 *Id.* at 402-03.

224 *Id.* at 396.

225 *Id.* at 403.

zen."[226] As such, gambling not only violated the Puritan work ethic but encouraged the poor to try and rise above their station and class.[227] The wealthy, therefore, sought to prohibit the lower classes from gambling in order to prevent any "rags to riches" stories. One manifestation of this concern was the restrictions placed on horse racing wagers. On-track wagering, available to those wealthy enough to pay the track's entrance fee, was considered legal, whereas off-track betting—for those not wealthy enough to pay the fee—was illegal.[228]

If the fear of gambling-enabled upward mobility answers why the dichotomy was created, however, it does not explain why it still exists. Even if we assume that most members of the upper class at the turn of the century were unaware that the odds in almost every gambling activity are against the gambler, today such knowledge is widely available on the internet.[229] Furthermore, large returns and upward mobility are available through a passively managed stock fund. Investing in such a fund would yield a greater increase in the long-term wealth of an average person than gambling. Therefore, investing poses more of a threat to prevailing social order than does gambling, yet it remains available to people of all income levels. All else being equal, wealthy citizens would probably prefer to insulate themselves and their wealth, but the proper policy given current understandings of probabilities and markets is to restrict the lower classes' access to wealth-creating debt and equity markets, not prevent them from engaging in negative-sum gambling activities.

Professor Hurt has argued that these moralistic arguments were also probably advanced by the emerging banking and securities industry to protect their own financial interests.[230] With a limited pool of funds available for speculation, the banking industry had to compete against established gambling operations for business.[231] This necessitated some method for distinguishing themselves from gambling businesses, and the moral arguments surfaced.[232]

Like Professor Hurt's classist explanation, this financial interest explanation can only plausibly justify the initial creation of the dichotomy. Indeed, Hurt herself does not necessarily ascribe any greater weight to either explanation. It is probable that when the moral criticism emerged, banks viewed gambling activities as competition. There is no reason why

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226 *Id.*

227 *Id.*

228 Hurt, *supra* note 8, at 403.

229 *See, e.g.*, Wizard of Odds, http://wizardofodds.com/games.

230 Hurt, *supra* note 8, at 403.

231 *Id.*

232 *Id.*

today's large financial institutions could not enter the field themselves, however, and financial firms should now look at gambling as a business opportunity. Some foreign firms already do; one British financial firm, Cantor Fitzgerald L.P., owns and operates a licensed sports book.[233] Additionally, some casinos already compete with banks by providing traditional financial services to their clients like extending credit, currency exchange, fund transfer, and check cashing.[234] Furthermore, financial institutions are well positioned to compete with other gambling companies. Nigel Payne, owner of British paradisepoker.net, noted that "trust is an immense factor" in gambling and "disreputable companies . . . won't last long."[235] This reliance on trust favors large, reputable financial institutions that Americans already trust to handle large sums of money,[236] and which have a tremendous amount to lose by operating fraudulent gambling websites.

The result of the foregoing analysis is that a couple plausible motivations for creating the dichotomy exist, but neither is a persuasive reason for its continued existence. The explanation for this unprincipled regime's perseverance is a tendency that Judge Robert Bork once warned against in the field of antitrust: an unquestioning acceptance of old ideas and policies.[237] Judge Bork warned that "[t]he less we know of how ideas actually took root and grew, the more apt we are to accept them unquestioningly, as inevitable features of the world in which we move."[238]

The prevailing justifications for the gambling prohibition are that gambling is immoral and causes social ills. It is not well-known that the prohibition "took root and grew" notwithstanding those justifications applying to investing as well. Nor is it well-known that the actual reasons for the prohibition's creation were self-interested and that those interests would be better served by gambling's legalization.

Because they are unaware of these facts, the American public has unquestioningly accepted the dichotomy, just as Judge Bork predicted. The basis for such acceptance is a trust that the justifications for the dichotomy were satisfactorily proved when the disparity began. Such trust is clearly misplaced because the justifications are not valid and could not be proven,

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233 *Id.* at 377.

234 Gottfried, *supra* note 106, ¶ 20.

235 *60 Minutes*, *supra* note 10 (interviewing Nigel Payne).

236 For example, Bank of America averaged $632 billion in deposits in 2005, and Merrill Lynch has over $1.5 trillion in its brokerage accounts alone. Press Release, Bank of America, Bank of America Reports Record 2005 Earnings of $16.89 billion, or $4.15 per Share (Jan. 23, 2006), http://newsroom.bankofamerica.com/index.php?s=press_releases&item=7255; Press Release, Merrill Lynch, Merrill Lynch Reports Record EPS and Net Earnings for Fourth Quarter and Full-Year 2005 (Jan. 19, 2006), http://www.merrilllynch.com/index.asp?id=7695_7696_8149_63464_63466_63662.

237 ROBERT H. BORK, THE ANTITRUST PARADOX: A POLICY AT WAR WITH ITSELF 15 (1978).

238 *Id.*

either 100 years ago or today. Acceptance was made easier because of the predominance of the elite in all forms of financial speculation, which gave such activities more superficial credibility than those classified as gambling.[239] This explanation for the dichotomy's persistence removes whatever credibility it retained after the previous three subparts. When a regime's creation is shown to be the product of self-interest and its perseverance the product of apathy, its only merit is that its "ideas are old; they carry whatever credentials time alone can confer."[240] And as Justice Black once put it, "[w]hen precedent and precedent alone is all the argument that can be made to support a . . . rule, it is time for the rule's creator to destroy it."[241]

E. *Taxability Alone Cannot Explain the Particular Hostility to Online Gambling*

Although how such an unprincipled dichotomy persisted for more than a century may be the most intriguing question about gambling policy, it is not the only one. Another is why the government has targeted certain gambling activities more harshly than others. There has been a general trend toward liberalizing some types of gambling like lotteries, but that trend has omitted other gambling activities like sports gambling and online gambling. The Department of Justice has taken the position that all online gambling is illegal under The Wire Act.[242] This is a harsher approach than the federal government has taken against traditional and online investing, but also harsher than traditional gambling, the regulation of which it delegates to the states or Indian tribes.[243]

Professor Hurt has argued the reason for singling online gambling out from traditional investing, online investing, and traditional gambling is that the latter three activities put money into the US economy while the former does not.[244] Investing, both online and offline, provides financing for U.S. corporations and generates fees and jobs for the financial intermediaries.[245]

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239 Hurt, *supra* note 8, at 403.

240 BORK, *supra* note 237, at 15.

241 Francis v. Southern Pacific Co., 333 U.S. 445, 471 (1948) (Black, J., dissenting); *see also* Oliver Wendell Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 469 (1897) ("It is revolting to have no better reason for a rule than that it was laid down in the time of Henry IV. It is still more revolting if the grounds upon which it was laid down have vanished long since, and the rule simply persists from imitation of the past.").

242 Hurt, *supra* note 8, at 414.

243 *Id.* at 375.

244 *Id.*

245 *Id.*

Additionally, it generates tax revenue for the government through dividends and capital gains taxes.[246] Traditional gambling in casinos and lotteries creates jobs and taxable revenue to help offset the ostensible social costs, but online gambling does not.[247] Online gambling, unregulated by the United States government and hosted by foreign corporations, neither provides jobs nor tax revenue, and competes with traditional gambling which does.[248] Hurt asserts that the government is therefore more supportive of the dichotomy in online activities because it cannot collect any revenue from online gambling.[249]

There are several problems with this justification for the harsher treatment of online gambling. First, it is incorrect that no additional tax revenue would accrue to the state or federal governments as a result of legalizing online gambling. If allowed, domestic websites would be created to offer online gambling and would be subject to United States taxes. Steve Lanni, CEO of the American gambling firm MGM Mirage, predicts that if online gambling was legal in the United States, his firm's revenue would double from $80 to $160 billion.[250] That is just one domestic gambling company. Additionally, there are intuitive reasons to believe that traditional brick-and-mortar casinos would enter and successfully compete in the online market. They have the ability to comp rooms and meals to online gamblers, something more costly for those without a brick-and-mortar presence. Brick-and-mortar casinos also possess a tremendous amount of credibility in the industry, which is important in an online environment.[251] Furthermore, taxes on domestic corporations would not be the exclusive source of revenue resulting from legalizing online gambling. Domestic online gambling companies would have to pay to advertise, which they are currently prohibited from doing.[252] Foreign corporations would also have to pay taxes. Nigel Payne calculates that had the American government regulated

246 *Id.*

247 *Id.*

248 Hurt, *supra* note 8, at 375.

249 *Id.*

250 *60 Minutes*, *supra* note 10; *see also* TelecomWeb, *supra* note 10 (citing a study claiming the United States government would receive $3 billion in additional tax revenues just from legalizing online poker).

251 *See supra* text accompanying note 235.

252 Hurt, *supra* note 8, at 435-36 (explaining that in 2004 the Department of Justice warned the National Association of Broadcasters that forced media outlets who accepted advertising from offshore gambling operations would be prosecuted); *see also 60 Minutes*, *supra* note 10. Such a ban has not been completely effective, however, because gambling websites still pay to advertise similarly-named websites that do not offer gambling in the hope of drawing them to their actual gambling site. For example, gambling website Paradisepoker.com advertises on television for an educational website, paradisepoker.net, with identical brand name and logos. *60 Minutes*, *supra* note 10.

internet gambling in 2004, it would have earned $1.2 billion in tax revenue from foreign corporations.[253]

Second, other taxable activities that could generate revenue remain illegal, so lack of tax revenue could not be the entire reason for online gambling's illegality. Prostitution, drugs like cocaine or marijuana, or market transactions in human organs could all generate tax revenue, and yet the government does not legalize them. Therefore, even if online gambling fails to generate taxable income, that could only be a partial explanation for the existence of the government's particularly harsh approach to online gambling.

In conclusion, sports futures are both gambling and investing under the gambling-investing dichotomy, which is problematic for a policy premised on a fundamental difference between the two. The policy's problem categorizing sports futures is not surprising, however, since there is no categorical distinction between the two activities. The dichotomy's century-long persistence is attributable to an apathetic acceptance by each generation, and the policy's anomalously harsh application to online gambling cannot be attributed to that activity's taxability. The next part applies the federal laws enacted in pursuance of the dichotomy to sports futures to see if they faithfully apply the dichotomy.

III. APPLICABLE FEDERAL LAW

Regulation of gambling activities is traditionally conceived as a state power under the Tenth Amendment,[254] but there are several federal statutes which may prohibit online gambling:[255] The Wire Act,[256] The Travel Act,[257] the aiding and abetting statute,[258] The Interstate Transportation of Wagering Paraphernalia Act,[259] and The Professional and Amateur Sports Protection Act.[260] Despite the potential applicability of all of these acts to online gambling, this Comment will focus on only The Wire Act and the aiding and abetting statute, as only these have been used to prosecute online gambling

253 *60 Minutes*, *supra* note 10 (quoting Payne as stating, "[T]he American states would have earned $1.2 billion in tax . . . . [W]e have volunteered to pay it because this is an industry that has to be regulated.").

254 Gottfried, *supra* note 106, ¶ 5.

255 Peter Brown, *Regulation of Cybercasinos and Internet Gambling*, 547 PLI/PAT 9, 21 (1999).

256 18 U.S.C. § 1084 (2000).

257 18 U.S.C. § 1952 (2000).

258 18 U.S.C. § 2 (2000).

259 18 U.S.C. § 1953 (2000).

260 28 U.S.C. §§ 3701-3704 (2000).

to date.[261] The CFTC's regulations could also apply to sports futures because the CFTC regulates futures contracts similar to sports futures. Subpart A analyzes sports futures under the prevailing interpretations of The Wire Act and the aiding and abetting statute, and Subpart B analyzes sports futures under the relevant CFTC regulations.

A. *Federal Statutes*

1. The Wire Act

Congress passed The Wire Act in 1961 to assist states in enforcing their anti-gambling laws.[262] The text of the statute[263] and subsequent court interpretations require the prosecution to show two elements: (1) the defendant used interstate wire facilities to transmit information that assisted in the placing of wagers; and (2) the defendant was engaged in the "business of wagering or betting."[264]

The first of these elements, the use of wire facilities to transmit betting information, raises the question whether the internet is a wire facility.[265] In *United States v. Cohen*, the Second Circuit addressed this issue.[266] The court affirmed the conviction of Jay Cohen, executive of Antigua-based World Sports Exchange, under The Wire Act for using both the telephone and Internet for receiving wagers.[267] Although some ambiguity still remains as to the sufficiency of internet communications for this element,[268] this ques-

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261 *See, e.g.*, United States v. Cohen, 260 F.3d 68 (2d Cir. 2001).

262 Pub. L. No. 87-216, § 2, 75 Stat. 491 (1961) (codified at 18 U.S.C. § 1084 (2000)).

263 The Wire Act reads in pertinent part: "Whoever being engaged in the business of betting or wagering knowingly uses a wire communication facility for the transmission in interstate of foreign commerce of bets or wagers or information assisting in the placing of bets or wagers on any sporting event or contest. . . ." 18 U.S.C. § 1084(a) (2000).

264 United States v. Truchinski, 393 F.2d 627, 630 (8th Cir. 1968); United States v. Ross, No. 98 CR. 1174-1(KMV), 1999 WL 782749, at *4-5 (S.D.N.Y. Sept. 16, 1999); United States v. Alpirn, 307 F. Supp. 452, 454 (S.D.N.Y. 1969).

265 Adrian Goss, *Jay Cohen's Brave New World: The Liability of Offshore Operators of Licensed Internet Casinos for Breach of United States' Anti-Gambling Laws*, 7 RICH. J.L. & TECH. 32, ¶19 (2001).

266 United States v. Cohen, 260 F.3d 68 (2d Cir. 2001).

267 *Id.*; *see also* People v. World Interactive Gaming Corp., 714 N.Y.S.2d 844, 852 (Sup. Ct. 1999) ("By hosting this casino and exchanging betting information with the user, an illegal communication in violation of The Wire Act . . . has occurred.").

268 David B. McGinty, *The Near-Regulation of Online Sports Wagering by* United States v. Cohen, 7 GAMING L. REV. 205, 210 (2003).

tion has been answered affirmatively in existing case law and this comment will not examine the merits of that answer.[269]

Assuming that other Circuits will agree with *United States v. Cohen*, the real question for information markets becomes whether Tradesports is "engaged in the business of betting or wagering."[270] Courts interpreting the business element of The Wire Act have required that the defendant be a bookie, meaning the defendant receives or takes bets.[271] At the same time, courts have explicitly refused to apply The Wire Act to mere bettors.[272]

United States v. Tomeo held that "[t]he statute deals with bookmakers—persons engaged in the business of betting or wagering. Bookies *take* bets, they receive them, they handle them."[273] Similarly, in *United States v. Anderson*, the Seventh Circuit concluded that The Wire Act only applied to bookies who take bets.[274] The court reversed a conviction under The Wire Act because there was no evidence that the defendant took any bets himself, only that he placed bets with the bookie.[275]

In *United States v. Baborian*, the United States District Court for Rhode Island refused to convict Robert Baborian under The Wire Act for being a professional gambler.[276] Baborian wagered with his bookie, Anthony Lauro, an average of $800 to $1000 per day from March through December, 1977.[277] The court held that the legislative history of The Wire Act showed that Congress intended for the act to apply to bookies and not gamblers, even those who gambled frequently and "with great sophistication."[278] The court did, however, convict the bookie Lauro, because there was evidence that he accepted wagers from Baborian.[279]

These cases illustrate that courts trying people under The Wire Act require the defendant to be a bookie. Tradesports' guilt under The Wire Act depends on whether the court finds it is a bookie. Courts are unlikely to find Tradesports is a bookie, because Tradesports does not trade on its ex-

269 For a discussion of this issue, see Goss, *supra* note 265, ¶¶ 19-23; McGinty, *supra* note 268, at 210-13; Gottfried, *supra* note 106, ¶¶ 46-50.

270 18 U.S.C. § 1084(a) (2000).

271 United States v. Sellers, 483 F.2d 37, 45 (5th Cir. 1973); United States v. Marder, 474 F.2d 1192, 1194 (5th Cir. 1973); United States v. Tomeo, 459 F.2d 445, 447 (10th Cir. 1972); United States v. Sagansky, 358 F.2d 195, 200 (1st Cir. 1966); Pic-A-State Pa., Inc. v. Commonwealth, Civ. A. No. 1:CV-93-0814, 1993 WL 325539, at *3 (M.D. Pa. July 23, 1993), *rev'd on other grounds*, 42 F.3d 175 (3d Cir. 1994); United States v. Baborian, 528 F. Supp. 324, 329 (D.R.I. 1981).

272 United States v. Anderson, 542 F.2d 428, 436 (7th Cir. 1976); *Baborian*, 528 F. Supp. at 329.

273 *Tomeo*, 459 F.2d at 447 (internal quotation marks omitted).

274 *Anderson*, 542 F.2d at 436.

275 *Id.*

276 *Baborian*, 528 F. Supp. at 331.

277 *Id.* at 326.

278 *Id.* at 328.

279 *Id.* at 331.

change, and therefore does not enter into any bets with others.[280] This is fundamentally different from bookies who will accept any bet offered them at the line, and should be dispositive under the courts' reasoning.

Additionally, Tradesports never has any of its money at stake on the outcome of a contest.[281] Because Tradesports does not have any of its money at stake, it is never susceptible to the losses of a traditional sports book, and its fees remain constant at approximately 1.60%. Ideally sports books would function in this way, by paying out what they take in and pocketing the "juice," but they remain susceptible to inaccurate handicapping[282] and in many cases stand to make more on one outcome than the other. It is therefore also a critical distinction between Tradesports and sports books that Tradesports never has any interest in the outcome of the game.[283]

2. Aiding and Abetting

Although Tradesports' actions may not violate The Wire Act,[284] it is possible that Tradesports could be tried for aiding and abetting others in violating of The Wire Act. Part (a) of the federal aiding and abetting statute allows for conviction as a principal of anyone who "aids, abets, counsels, commands, induces or procures" an offense against the United States.[285]

The obvious pre-requisite for a conviction of aiding another in the commission of a crime is that the prosecution must show that a crime was committed under another statute.[286] It is not necessary, however, that the

280 Tradesports Most Asked Questions, http://www.tradesports.com/aav2/rulesAndFaqs.jsp?helpPage=mostAsked#10 (last visited Sept. 10, 2006).

281 Remember that the sum of the wagers is equal to the contract price. If a $10 contract was trading at 29.00, it would cost buyer A $2.90 to buy it, and cost buyer B $7.10 to buy its mutually exclusive counterpart. The holder of the contract that correctly predicted the outcome would receive $10, and Tradesports would not have been liable for either outcome.

282 Bookies' susceptibility to inaccurate handicapping significantly distinguishes sports books from traditional casinos. In casino games, the odds are always in the casino's favor, while a sports book's advantage is contingent on the skill of the handicapper. Levitt, *supra* note 32, at 223. It is of course possible that bookies are not trying to place the line at equilibrium, but are trying encourage bettors to make poor bets, exacerbating their exposure. *See supra* note 119.

283 *Cf.* Abramowicz, *supra* note 5, at 948 (explaining how the Iowa Electronics Market's lack of financial interest in its contracts distinguishes it from a casino).

284 *See* United States v. Anderson, 542 F.2d 428, 430 (7th Cir. 1976); United States v. Alpirn, 307 F. Supp. 452, 452-54 (S.D.N.Y. 1969).

285 18 U.S.C. § 2(a) (2000).

286 WAYNE R. LAFAVE, CRIMINAL LAW § 13.1(e) (4th ed. 2003).

principal have been convicted of that crime.[287] The requirement that a crime be committed is so well accepted that some courts have classified it as "hornbook law."[288] Thus, in order to convict Tradesports, or any other on-line information market, the prosecution must show that Tradesports aided traders who violated The Wire Act. Since courts have explicitly refused to apply The Wire Act to those who simply place bets, even if they do so on a consistent basis,[289] a trader violating The Wire Act must be a bookie.[290]

There is a very logical reason why bookies would not use Tradesports to operate their business. Bookies make their money by forcing bettors to pay the "juice" and then minimizing their exposure, not by out-predicting bettors. The only thing that the contract-pricing system on Tradesports will allow is payouts proportionate to the odds; it does not allow one party to charge another "juice." Anyone seeking to make money on Tradesports must bet that they can out-predict the other traders,[291] something that bookies seek to avoid. Therefore, bookies would not use Tradesports, and by allowing bettors to trade on its exchange, Tradesports is not aiding and abetting violations of The Wire Act.

The government's inability to prosecute Tradesports under these statutes is a deviation from the theory of the gambling-investing dichotomy. After all, Tradesports is gambling, which the dichotomy and The Wire Act claim to prohibit. The next part examines whether investing regulations are more consistent with the dichotomy's ideals.

B. *Commodity Futures Trading Commission*

In addition to The Wire Act, another possible source of federal regulation is the CFTC.[292] Congress created the CFTC in 1974 and expanded its

287 United States v. Motley, 940 F.2d 1079, 1081 (7th Cir. 1991); United States v. Powell, 806 F.2d 1421, 1424 (9th Cir. 1986); United States v. Ruffin, 613 F.2d 408, 412 (2nd Cir. 1979).

288 *Motley*, 940 F.2d at 1081; *Ruffin*, 613 F.2d at 412.

289 United States v. Anderson, 542 F.2d 428, 436 (7th Cir. 1976); United States v. Alpirn, 307 F. Supp. 452, 452-54 (S.D.N.Y. 1969).

290 United States v. Sellers, 483 F.2d 37, 45 (5th Cir. 1973); United States v. Marder, 474 F.2d 1192, 1194 (5th Cir. 1973); United States v. Tomeo, 459 F.2d 445, 447 (10th Cir. 1972); United States v. Sagansky, 358 F.2d 195, 200 (1st Cir. 1966); Pic-A-State Pa., Inc. v. Commonwealth, Civ. A. No. 1:CV-93-0814, 1993 WL 325539, at *3 (M.D. Pa. July 23, 1993), *rev'd on other grounds*, 42 F.3d 175 (3d Cir. 1994); United States v. Baborian, 528 F. Supp. 324, 329 (D.R.I. 1981).

291 It is by forcing participants to out-predict each other that information markets are superior information aggregation mechanisms; any market that did not require this would not be an information market. *See* Hahn & Tetlock, *supra* note 1, at 266.

292 *See id.* at 267; Hurt, *supra* note 8, at 396.

responsibilities in 2000.[293] The CFTC's mission is to monitor and regulate commodity futures trading in the United States.[294] A federal statute makes it unlawful to trade any "contract for the purchase or sale of a commodity for future delivery unless such transaction" occurs on and subject to the rules of a market approved by the CFTC, and the transaction is evidenced by specific written documentation.[295] Thus, Tradesports could operate within the United States if either it is not trading contracts of a "commodity for future delivery," or it is an authorized exchange with authorized contracts. [296]

The threshold question in evaluating Tradesports' legality under CFTC regulations is whether its contracts are for a "commodity for future delivery" as defined in the Commodity and Futures Modernization Act.[297] If they are not, then they would be neither regulated nor prohibited by the CFTC.[298] The definition of commodity under Commodity Exchange Act is extremely broad, including "all services, rights, and interests in which contracts for future delivery are presently or in the future dealt in."[299] Under this broad definition, sports contracts appear to be a commodity because they are the sale of an interest in the outcome of a sporting event.

Because sports futures would be considered commodity contracts, Tradesports would need to be a licensed exchange to operate legally in the United States. Exchanges become authorized by filing an application to the CFTC, showing that the exchange meets the requirements in the Commodity Exchange Act.[300] In 2004, the CFTC approved the first exclusively-online contract market, Hedgestreet,[301] for operation as a contract market.[302] Tradesports has not applied for CFTC approval, but the approval of

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293 Commodity Futures Trading Commission, About the Commodity Futures Trading Commission, http://www.cftc.gov/cftc/cftcabout.htm?from=home&page=aboutcftcleft (last visited Sept. 10, 2006).

294 *See id.*

295 7 U.S.C. § 6(a) (2000).

296 *Id.*

297 *Id.*

298 *Id.*

299 *Id.* § 1(a)(4).

300 *Id.* § 8(a). These requirements are: Prevention of Market Manipulation, Fair and Equitable Trading, Trade Execution Facility, Financial Integrity of Transactions, Disciplinary Procedures, Public Access, and Ability to Obtain Information. 7 U.S.C. § 7(b) (2000).

301 "HedgeStreet is a person-to-person marketplace where you can speculate on economic events such as the price of gas, gold, housing and much more." How HedgeStreet Works, http://www.Hedgestreet.com/howitworks.

302 Letter from Jean A. Webb, Sec'y, Commodity Futures Trading Comm'n, to Gregory J. Robbins, Counsel for Hedgestreet (Feb. 18, 2004), http://www.cftc.gov/files/opa/press04/opahedgestreet_designation_order.pdf.

Hedgestreet indicates that Tradesports could organize itself in a way that would allow for approval as a contract market.

Tradesports would also need to have its contracts approved, however, because the CFTC regulates the type of contracts that may be traded on authorized exchanges.[303] Exchanges are able to self-certify their contracts to the CFTC, but remain liable to suit for non-compliant contracts.[304] All contracts listed must conform to a public interest requirement enunciated in the Commodity and Futures Modernization Act.[305] This public interest requirement mandates that a contract "provide a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair and financially secure trading facilities."[306]

To get sports futures approved, Tradesports must show that sports futures are "affected with a national public interest" by providing for hedging against price risk or disseminating or discovering pricing information through trading.[307] The CFTC is unlikely to approve sports futures under this standard.[308] Sports futures are unlike any other future contract approved by the CFTC, because all other contracts have an underlying asset with a tangible price. The underlying asset for sports contracts is not a tangible asset that can be bought or sold like a bushel of wheat or gallon of gasoline. Even futures contracts for stock market indexes have an underlying asset: the shares of stock in that index. Without a tangible asset with a dollar-denominated price, it is unlikely that the CFTC will find that sports contracts can hedge against price risk or disseminate and discover price information.

In sum, current federal law does not prohibit sports futures under gambling legislation, but instead prohibits sports futures under investment regulation.[309] It is a bad sign for any policy regulating two purportedly dif-

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303 7 U.S.C. § 7a-2(c) (2000).

304 *Id.*

305 "A board of trade shall submit: . . . (4) . . . additional evidence, information or data relating to whether the contract meets, initially or on a continuing basis, any of the specific requirements of the Act, including the public interest standard contained in [7 U.S.C. § 5] and whether the contract reasonably can be expected to be, or has been, used for hedging and/or price basing on more than an occasional basis . . . ." Commodity Futures Trading Commission, Guideline No. 1: Interpretative Statement Regarding Economic and Public Interest Requirements for Listing Contracts, *available at* http://www.cftc.gov/dea/analysis/deaguide1.htm (last visited Sept. 10, 2006).

306 7 U.S.C. § 5(a) (2000).

307 *Id.*

308 Posting of Chris F. Masse to Conglomerate, http://www.theconglomerate.org/2005/07/blurring_the_li.html (July 22, 2005, 15:51CDT) ("[T]he CFTC will designate event-driven futures exchanges that float weather and financial contracts only. [Tradesports] will have no full-scale American competitors in the foreseeable [sic] future.").

309 *See supra* Part II.A-B for an explanation of why sports futures are both gambling and investing.

ferent activities that laws targeting one affect the other, but it is especially devastating when that policy is predicated upon an ability to distinguish between the two. Part IV proposes a better approach.

IV. GETTING BEYOND THE GAMBLING-INVESTING DICHOTOMY: A COST-BENEFIT ANALYSIS OF SPORT FUTURES

The gambling-investing dichotomy is predicated on an unjustified faith in the ability of regulators to distinguish between the two activities. The government's regulation of gambling through investing regulations signals either regulators' inability to distinguish the two, or their apathy towards the dichotomy's goal of disparate treatment. In either case, the regime is unsound. A better approach evaluates the benefits and costs of sports futures.

A. *The Social Benefits of Sports Futures are Identical to Those of Online Investing*

If sports futures can be regulated to keep any associated costs lower than the associated benefits, it behooves the United States to legalize them. Due to the illegality of online gambling, it is difficult to estimate the size of any expected costs or benefits related to it. The analysis can proceed, however, assuming that online investing represents an acceptable balance of costs and benefits. If it did not, rational legislators would outlaw it. Accordingly, if regulated sports futures present the same costs and benefits, lower costs and the same benefits, or the same costs and greater benefits than regulated online investing, sports futures should be legalized and regulated.[310]

The only activity that can be usefully compared to regulated sports futures is regulated online investing.[311] Unregulated online investing does not provide a useful comparison because the government has not approved that activity, and therefore it is not apparent that it has a satisfactory balance of costs and benefits with which to compare sports futures. Unregulated sports futures do not provide a useful comparison because it is unrealistic to expect that sports futures would be legalized without regulation. Furthermore, it would be inequitable to compare one activity with the benefit of regulation to another activity without the same benefit. Because the costs and

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310 The volume of these two activities might vary greatly, so the comparison here is per dollar wagered or invested.

311 *See* Hurt, *supra* note 8, at 430-31.

benefits of sports futures and online investing are equal, sports futures should be legalized.

The legalization of sports futures would create three potential benefits. First, it would encourage offshore information markets like Tradesports to operate locally, generating tax revenue for the United States and jobs for local economies.[312] This would likely not be a trivial amount of tax revenue, since sports gambling has been identified as "one of the 'largest untapped sources of potential tax revenue in the nation.'"[313] Sports futures may also create jobs outside of companies operating sports futures markets. The ability to profit from sporting events should create a greater interest in professional sports and generate greater media coverage of those events.[314] This increased interest, in turn, should cause growth in media firms.[315] One clear example is the benefit accruing to ESPN, an all-sports cable network, as a result of the dramatic increase in fantasy sports leagues.[316]

Second, sports futures provide another investment mechanism for the American public, allowing for greater diversification. Diversification allows investors to reduce the variance in their returns without reducing their expected return, but is difficult to achieve when dealing with all financial instruments because many move in tandem with each other and the market. Enabling people to legally invest in non-economic assets like sports futures allows for additional diversification, which should generate more consistent returns under Modern Portfolio Theory.[317] Furthermore, the labor-intensive process of investing in weekly sports futures can be avoided by using longer-term securities. For instance, a diversification-seeking investor could enter a futures contract that pays $1 for every win the Yankees amass over the next five seasons.[318] If traders collectively thought the Yankees would win half of their games during that period, the expected value in five years would be $405, which, when discounted back to present value, would provide a trading price today. The result is effectively a zero coupon

312 *See supra* Part II.E for an explanation of how online gambling will create revenue for the American economy.

313 Hurt, *supra* note 8, at 399 n.188 (quoting RICHARD O. DAVIES & RICHARD G. ABRAMS, BETTING THE LINE 2 (2001)).

314 *Id.* at 390.

315 This growth may not be socially beneficial, however, if it simply mirrors the decrease in other industries.

316 Chris Ballard, *Fantasy World*, SPORTS ILLUSTRATED, June 21, 2004, at 80.

317 *See* MALKIEL, *supra* note 155, at 206-11; Hazen, *supra* note 31, at 161.

318 This is unlike the binary sports futures traded discussed above. Rather than being worth nothing or everything, its value at maturity varies within a certain range according to the size of a certain number. In this case it would be between $0 if the Yankees do not a game in the next five years, and $810 if they won every game during that period. For more information on conditional information markets, see generally Abramowicz, *supra* note 5, at 952-58.

bond,[319] the returns on which fluctuate according to a non-economic variable like a sports team's performance.[320]

Third, trading sports futures and gambling in general are value-creating transactions.[321] Sports gambling is estimated to be a $380 billion dollar industry in the United States,[322] and a 2004 Gallup poll found that 66% of Americans had gambled within the last twelve months.[323] Clearly, a high percentage of Americans want to put money at risk with a negative expectation. Those who do so must derive sufficient utility from the activity to compensate for the amount they expect to lose on each bet, or they would never make the bet.[324] As such, the expected loss for each wager should be thought of as consideration for the utility derived from participating in the activity. American law typically assumes that the parties to a voluntary transaction are capable of assessing the value of consideration, and it honors their decisions. Two examples of this approach are allowing people to smoke cigarettes and eat fast food, both of which have been shown to have harmful effects.

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319 A zero coupon bond is a debt instrument that does not pay periodic interest payments like traditional bonds. MALKIEL, *supra* note 155, at 302. Instead, the return on a zero coupon bond comes from the buyer paying a price lower than the face value of the bond. This difference in price corresponds to the amount of interest the purchase price would earn over the bond's duration at the prescribed interest rate. In other words, the purchase price is the present value of the bond's face value, discounted at the relevant interest rate. For example, a 10%, 10-year, zero coupon bond with a $10,000 face value would issue for $3,855.50. This purchase price, if invested at 10% annually for 10 years would grow to be $10,000.

320 Interest will still affect the returns on this long-term sports future, but to a lesser degree than it affects the returns on a zero coupon bond. Interest rates will influence the current price of the sports future or bond because they are incorporated into the discount rate. All else being equal, this will alter the returns to investors in either sports futures or bonds. The return on a sports future, however, will be less influenced by the interest rate than a bond because the sports futures' value at maturity fluctuates. Unlike bonds whose price at maturity is fixed, the price at maturity of a sports future varies according to a non-economic factor like the success of the New York Yankees. Therefore, the bond's return is wholly determined by the interest rate while the return on the sports future is determined by both the interest rate and a team's performance.

321 *See* Hurt, *supra* note 8, at 390 ("Both sports betting and stock trading have some degree of entertainment value."); Statman, *supra* note 207, at 11.

322 Hurt, *supra* note 8, at 400.

323 Melissa Schettini Kearney, *The Economic Winners and Losers of Legalized Gambling*, 58 NAT'L TAX J. 281, 281 (2005).

324 *Cf.* Lloyd R. Cohen, *The Lure of the Lottery*, 36 WAKE FOREST L. REV. 705, 714-15 (2001) (arguing that people buy lottery tickets for the chance to dream about a windfall and a better life, not for a positive expected return). One caveat is that pathological gamblers may not employ a logical decision-making rationale, but recent data suggest that only 1% of Americans are afflicted with that disorder. Gottfried, *supra* note 106, ¶ 27.

Of these three benefits, two are identical to those from online investing and one may be greater than its counterpart from online investing.[325] Sports futures create jobs in sports futures companies and create tax revenue for the government just as investing does. They may also create jobs in the media at stations like ESPN, just as investing has created jobs at networks that cover the markets like MSNBC. Sports futures are also voluntary transactions like investing, and therefore are value-creating. In addition, sports futures may actually provide a greater benefit than other investing activities because they introduce an entirely new area of investment with which to diversify an investment portfolio. Thus, the benefits of sports futures are at least equal to those provided by online investing and could possibly be greater.

B. *The Social Costs of Sports Futures are Identical to Those of Online Investing*

Since the three benefits of sports futures are identical to or greater than those from regulated online investing activities, the necessary inquiry here is whether the costs associated with regulated sports futures would be greater than the costs of regulated online investing. The costs that could be caused by sports futures are those traditionally associated with online gambling: a disproportionate increase in fraud, underage gambling, addiction, and money laundering.[326]

CFTC regulations could alleviate any serious concerns of fraud. The CFTC requires every licensed exchange to have its own fraud monitoring system.[327] This is effectuated by an adequate surveillance system through real-time monitoring. With such monitoring, the chance of fraud in the execution of these contracts would be reduced to the level of other investing activities.

The concerns over fraud in the execution of sports futures may also be lower than in online casinos. Online gaming sites employ computer algorithms to simulate random odds, rather than actually randomly dealing cards, and therefore opponents of online gambling believe online casinos may actually be giving players lower odds than advertised.[328] Sports contracts do not involve simulating random chance so they would not be sus-

325 The only benefits of online investing relevant to this discussion are those created by all legal forms of investing. The wealth-creating or capital raising features of equity markets are irrelevant, because the government is willing to legalize investment activities without them.

326 Gottfried, *supra* note 106, ¶ 14; Hurt, *supra* note 8, at 425-32. *See supra* Part II.A for an explanation of why critics associate these fears with online gambling.

327 7 U.S.C. § 7(b)(2) (2000).

328 Hurt, *supra* note 8, at 428.

ceptible to this criticism. Additionally, Tradesports has no interest in the outcome of any event so there is no incentive for them to engage in fraud regarding payoffs.

There is the ever-present concern that sports teams could alter the outcome of the game to alter the value of the contracts. This activity, called point-shaving because a favored team could intentionally win by less than the line—thereby winning on bets against themselves but still winning the game—is unlikely for several reasons. First, it is already independently monitored by the sports leagues themselves. Additionally, point-shaving is already illegal, and therefore it should be no more of a concern than someone destroying another's crops to devalue commodity prices. Second, sports futures are distinguishable from any situation involving point shaving in the past because there is no bookie. A bookie has more money riding on a game than any individual bettor, and that gives bookies the greatest incentive to manipulate the game in their favor. Since Tradesports does not have any stake in the outcome of the game, and all those with a stake are individual traders, there is no party with the incentive of a bookie. By removing the person with the greatest incentive to cheat, sports futures exchanges lower the likelihood of point-shaving. Third, participants in any game can be prohibited from gambling on that game by forcing Tradesports to monitor who gambles on its site, just as it would verify the age of its traders. In the event the contest was found to be rigged by a bettor, the contracts could be rescinded and the money returned.

Opponents of online gambling also point to the risk of underage gambling. In countries where online gambling is legal, however, online gambling websites have required players to send in some type of verification of age before they are licensed to participate.[329] This is more restrictive than what most minors face at traditional casinos, where the primary concern is that minors will win money rather than lose money.[330] A similar age verification system at Tradesports could effectively eliminate the underage gambling concern. Gambling by minors is unlikely to be a major problem, though, because trading online requires a credit card, which poses certain difficulties for minors.[331] If minors are gambling with their own credit card, they would need an independent stream of income to pay off their losses.[332]

329 *Id.* at 423; s*ee also 60 Minutes*, *supra* note 10 (quoting Nigel Payne: "[A] 16-year-old has got to give me four or five pieces of information about him relative to his bank account, his personal details, where he lives and other things. So I can be 99 percent comfortable that this 16-year-old doesn't even get through my front door.").

330 Hurt, *supra* note 8, at 424. One twenty year-old poker player, after gambling for hours, was only expelled from Foxwoods casino after attempting to purchase alcohol. Daniel G. Habib, *Online and Obsessed*, SPORTS ILLUSTRATED, May 30, 2005 at 66.

331 Gottfried, *supra* note 106, ¶ 34; Hurt, *supra* note 8, at 424.

332 Gottfried, *supra* note 106, ¶ 34.

If minors are using their parents' credit cards to gamble, the losses would appear on the parents' monthly statement or their parents would receive the winnings as the cardholder.[333] Neither result leaves much incentive for minors to gamble.

Opponents of online gambling also argue that it would increase the number of people with gambling addictions. This criticism may be accurate, but it is too narrow. Online investing can also cause pathological addiction to gambling.[334] Therefore, anything in the online environment that exacerbates pathological gambling in online gamblers could also exacerbate pathological gambling in online investors.[335] Online investing is no more conspicuous than trading sports futures, so if the latter makes it easier to avoid alerting family and friends, then so does the former. Similarly, if a lack of tangible assets increases problem gambling, then online investing is no better than sports futures because there are no tangible assets inherent to either activity. The one thing that may make sports futures worse than online investing is that Tradesports is open twenty-three hours a day, whereas other markets close. This is not as significant as it might seem, however, because the internet allows online investors to trade on any market in the world. Trading on only four markets—New York Stock Exchange, the London Stock Exchange, the Hong Kong Stock Exchange, and the Tokyo Stock Exchange—an online investor would be able to trade for nineteen and one-half hours a day.[336] Since traders need to sleep at some point, this effectively allows them to trade during all of their waking hours.

The problem of money-laundering is not unique to online gambling, but could also easily be effectuated during traditional gambling and investing activities.[337] Money-laundering "thrives on poor regulatory oversight and anonymity."[338] Accordingly, Congress combated the problem with the Bank Secrecy Act,[339] which requires casinos and financial institutions to report the name and social security number of anyone who spends more than $10,000 or receives $2,500 in cash or extension of credit.[340] The United States has exacerbated the online money-laundering problem by

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333 *Id.*

334 See *supra* Part II.C for a more thorough description of how investing and gambling can each lead to gambling addiction.

335 See *supra* Part II.A for a detailed discussion of the features of the online environment thought to exacerbate gambling addiction.

336 *See* StocksQuest, World Markets' Hours of Operation, http://investsmart.coe.uga.edu/C001759/world/world_nf.htm (last visited Sept. 10, 2006).

337 Hurt, *supra* note 8, at 427.

338 Gottfried, *supra* note 106, ¶ 24.

339 31 U.S.C.A. §§ 5311-5314, 5316-5332 (West 2006); 12 U.S.C.A. §§ 1829(b), 1951-1959 (West 2006); 31 C.F.R. § 103 (2006).

340 Hurt, *supra* note 8, at 427.

forcing domestic credit companies to abandon online gambling operations.[341] Online gamblers must now use a more circuitous route to get their money offshore, allowing criminals more layers through which to launder the money.[342] These transactions are also conducted with electronic money, which unlike credit cards, does not have to leave a transaction record.[343] So not only do money-launderers have more opportunities to launder their money because more transactions are required, but each transaction provides a better opportunity because the records are less complete.[344] Were Tradesports regulated and allowed to operate domestically, credit cards could be used and records would be kept, the strictures of the Bank Secrecy Act would apply, and the problem would be no worse than online investing.

The foregoing cost-benefit analysis reveals that the marginal benefits are at least as great as online investing activities, and the costs are not any greater. As such, the legal policy applied to online investing should be applied to online gambling as well. The CFTC should remove the public interest requirement and apply the other investment regulations currently applied to futures markets to sports futures. This change will allow the United States to capitalize on "one of the 'largest untapped sources of potential tax revenue in the nation,'"[345] and ensure the marginal costs are not greater than those associated with online investing.

CONCLUSION

The United States predicates its regulation of speculating activities upon a supposed distinction between gambling and investing. Many scholarly works, this Comment included, have argued that such a distinction does not make sense because the activities are too similar to distinguish categorically. By satisfying the definitions of both activities, sports futures expose this flaw in the dichotomy. The dichotomy persists despite its failure, however, because Americans incorrectly assume that a fundamental difference between gambling and investing was proven at its inception.

This dichotomy manifests itself in a desire to prohibit gambling and regulate investing. The primary federal gambling prohibition is The Wire Act, which was drafted to prevent interstate sports wagering. Yet despite the dichotomy's central tenet of prohibiting gambling, as well as The Wire

341 Gottfried, *supra* note 10, ¶ 22; Hurt, *supra* note 8, at 427-28.

342 Hurt, *supra* note 8, at 427-28.

343 Gottfried, *supra* note 106, ¶ 22.

344 *Id*.

345 Hurt, *supra* note 8, at 399 n.188 (quoting RICHARD O. DAVIES & RICHARD G. ABRAMS, BETTING THE LINE 2 (2001)).

Act's declared purpose to do the same, sports futures are not prohibited under The Wire Act. Instead, they are illegal because the CFTC's investment regulations impose a public interest requirement on all futures contracts. The government, therefore, prohibits gambling not through gambling legislation, but through investing regulations. This inability to tailor regulations specific to each activity is merely a manifestation of the inherent flaw in the dichotomy.

The dichotomous regime prevents the United States from realizing the benefits of sports futures, such as additional tax revenue and the increased diversification stemming from a non-economic investment. These benefits are as great, or greater, than those created by online investing activities. Furthermore, the social costs associated with sports futures are no greater than those of online investing. A relative cost-benefit analysis of these two activities shows that if online investing is legal, sports futures should be legal as well.