



The Odds Are Good That Online Gambling Will Continue to Thrive -- But at What Price?

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Online poker is on a winning streak. According to research firm River City Group, Internet poker alone is a \$2 billion-a-year industry with a million players monthly. ComScore Media Metrix -- which measures all U.S. Internet users at home, work and college locations -- reports more than 29.1 million unique visitors to online gambling sites in April, out of a total audience of 165 million.

And, according to a recent survey from The University of Pennsylvania's Annenberg Public Policy Center, card playing for money has increased among males between the ages of 14 and 22. In 2004, 11.4% of in-school male youth reported betting on cards at least once a week, up from 6.2% in 2003; furthermore, 11.4% of these weekly card players are likely to gamble on the Internet. In addition, 43.2% of players who bet money weekly on cards were under 18, according to the Annenberg survey.



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The most popular online poker sites, as compiled by CasinoCity.com, include PartyPoker.com and Pacific Poker, based in Gibraltar; PokerRoom.com and Empire Poker, based in Kahnawake, Canada; and Poker World Online Cardroom, based in Jamaica. Meanwhile, PartyGaming, the parent of PartyPoker.com, is planning to go public this week on the London Stock Exchange in an IPO valued at \$9 billion. According to press reports, the company reported a profit of \$371 million in 2004 on revenue of \$601.6 million. For the first quarter of 2005, PartyGaming reported a profit of \$125 million.

Observers agree that the numbers are impressive -- at least for the leaders. "It's a big business, widely distributed and badly regulated," says Wharton legal studies professor [Dan Hunter](#). Indeed, the proliferation of online gambling operators such as the Gibraltar-based PartyGaming has opened a host of public policy, legal and e-commerce debates: What is legal? Do current laws on the books have any impact on Internet gambling? Can U.S. authorities realistically cut off Internet sites that operate offshore? Is it up to states to legalize online gambling?

"There's a lot of concern about whether this is legal, especially when it's a form of gambling that's accessible to adolescents," says Daniel Romer, research director of Annenberg's Adolescent Risk Communications Institute. He notes that casinos are limited to people over 21 years of age, and lottery tickets are sold to those 18 and older. While some online gambling sites check age, underage players can simply bluff about their real birth dates.

It all adds up to a growing gambling paradox in the U.S., where policymakers are trying to put the kibosh on online gambling sites even as games of chance are a part of daily life. Lottery tickets are sold in vending machines, and states looking to boost revenue are launching casinos at a rapid clip. Poker-game broadcasts abound on cable television: "Celebrity Poker Showdown," "Poker Superstars Invitational Tournaments," "National Heads-Up Poker Championship," "Ultimate Poker Challenge" and "World Poker Tour" are just a few. Toss in games found online, and poker itself could become a 24-hour obsession with the potential to lead to other forms of gambling.

"We have a strange relationship with gambling," says Hunter. "Not only do many states rely on it for their revenues -- a situation that generates its own weird political economies -- but we don't really like the state [watching over] what we do with our free time and money. Against this, we have reasons why gambling might be regulated, including moral reasons, social problems, or protection of certain classes who are uniquely unable to deal with the issues that gambling presents. So, in the abstract, gambling is a vexed arena."

One thing is certain: Curtailing Internet gambling won't be easy. "It would be difficult to stamp out online gambling," says [Kevin Werbach](#), legal studies professor at Wharton. "U.S. states have tried, and there have been various federal bills proposed, but the activity continues to grow. As long as gambling is legal somewhere, it's difficult to ban it based on its illegality elsewhere."

Regulating Beyond Borders

In the short-term, the predominant public policy response to online gambling is to target major site operators and make examples of them with stiff penalties. Should the U.S. launch stings designed to shut down the sites when agencies like the Federal Bureau of Investigation don't have jurisdiction? Should these online gambling sites be allowed in the U.S., but be regulated and taxed? The United Kingdom recently took such a step. "In the U.K., the theory is to regulate [online gambling] to prevent underage players," says Romer.

Keith Whyte, executive director for the National Council on Problem Gambling, notes that legality and enforcement are two different things. "You can say online gambling is illegal, but if you can't enforce [the law] it doesn't matter," he says.

In general, individual states in the U.S. regulate games of chance within their borders, and the rule of thumb is that gambling is illegal unless it is specifically legalized through the law. The problem with that approach is that Internet gambling is borderless. "There's the regulatory difficulty of stopping activity that occurs legally on a server in Antigua, and there's the enforcement difficulty of finding the activity happening locally without banging on the basement-den door of every guy in Philadelphia," says Hunter. "Then there is the issue that we don't have very good data about the usage figures, largely because this is a distributed environment."

Romer says the main solution may be just to make online gambling legal, regulate it and put safeguards in place. However, that's easier said than done. Typically, gambling is a state issue and jurisdiction is unclear. In addition, several interests are at stake. States, which are increasingly reliant on gambling revenue from casinos and horse racing tracks, won't be happy about online competition.

Ultimately, online courts and legislatures in the U.S. will dictate online gambling policy. Last year, CasinoCity.com sued the Justice Department over taking advertising from online gambling sites offshore. In April, the World Trade Organization ruled in favor of Antigua over a 2003 complaint about the U.S.'s "total prohibition" of cross-border third party gambling services. The federal government forbids using wire communications to place bets, a law that may impact online gambling. Meanwhile, North Dakota floated a bill to make online gambling legal only to see it defeated in the state senate.

Word-of-Mouth Success

From a business perspective, online gambling sites have all the hallmarks of a thriving e-commerce business, says Werbach. "Gambling lends itself perfectly to e-commerce. It involves connecting people, not physical goods, which the web does exceedingly well. The overhead for an online gambling site is tiny compared to a real-world casino -- they don't need any of the real estate, dealers, or security."

According to Werbach, the only real hurdle is trust. "Users must be convinced they aren't being cheated; it's harder to offer that confidence when the players don't see each other face to face," he notes.

Nevertheless, there are enough repeat customers to create strong word-of-mouth, or "viral," marketing and reel in new players. According to the Annenberg study, gambling among college and high school students has proliferated due to social networks where friends invite friends. "Because online gambling is illegal, these sites can't market through legitimate means," says Andy Sernovitz, CEO of the Word of Mouth Marketing Association, or WOMMA. "It's not like they can buy a billboard and say 'gamble here.'"

The social aspects of online gambling coincide with an effective marketing strategy. Sernovitz says successful word-of-mouth marketing consists of finding influencers in a group, giving them something to talk about, making the message easy to pass along and then tracking results. The popularity of poker was stoked by the massive exposure to the game by television, says Sernovitz. Word of mouth took it from there. In the case of online poker, these messages can move seamlessly through emails, weblogs, conversation and instant messaging.

Indeed, the big question is whether web gambling will become such a hit that it will threaten traditional casinos. Wharton professor [Witold Rybczynski](#), who has studied Las Vegas's transformation into an entertainment mecca, doesn't see online gambling as a viable threat to brick-and-mortar rivals yet. "My guess would be that the impact of online gambling on place-based gambling will be analogous to the impact of online retailing on malls," he says. "That is, it will be small. Sitting alone in front of a computer cannot compare with the total urban experience of Las Vegas, which includes entertainment, crowds, excitement, and so on. Las Vegas has gone far beyond simply gambling, and is basically an entertainment/convention city." Werbach agrees. "There is no substitute for looking another player in the eye, and gauging his or her response, so online casinos will never completely replace their physical counterparts. But there's still a huge potential market out there."

While online casinos may not be an initial threat to their real-world counterparts, the Internet is likely to force changes. "Just as Amazon.com forced physical-world bookstores to focus on the customer's experience, online gambling will force casinos to emphasize the unique aspects of what they do," says Werbach. That fact may make it harder for other cities and states to explore gambling as a revenue source, adds Rybczynski. "It's no longer simply a question of lining up slot machines on the floor and providing a tired floor show," he says.

To be sure, the battle is just beginning. Assuming the U.S. legalized online gaming, some traditional casinos might eventually decide to claim their own space on the Internet. "These casinos have brands to protect, and I bet that would translate online," says Whyte.

Future Problems

Whether online gaming becomes legal will depend on how lawmakers' perceptions change. The biggest worry for Internet gambling is that there will be a new generation of problem gamblers, says Whyte. Notes Romer: "When you gamble online, transmitting money is easier and you don't know how much you are losing. My concern is that kids are getting into hock on the web and maxing out credit cards." He says Annenberg will ask about gambling debts in future surveys. "Right now we just don't know. There are only anecdotes. For every guy making a lot of money, there are losers."

Whyte typically hears from those who lose too much. He says that callers into his national hotline are increasingly mentioning that poker is a problem for them. However, the National Council for Problem Gamblers doesn't segregate calls based on whether players came from online or elsewhere so he can't tell if the Internet has compounded problem gambling. "We don't really get into how you access gambling," says Whyte. "That's like asking an alcoholic what kind of vodka he drinks."

To Hunter, that lack of data about online gambling and its effects is part of the problem. In lieu of demonstrated effects, policy regarding online gambling is built on "hunches, supposition, moral-highground-grabbing, and political infighting ... A better approach would be to spend more time and effort getting a sense of what this market looks like, whether it is causing particular types of problems," says Hunter. "At the moment it is so poorly supported from the empirical side that I view any regulator's pronouncement with great suspicion. Better data will lead to better legislation in this case."

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