



*cutting through complexity*

Thursday 11th April 2013

# Report



KPMG eGaming  
**SUMMIT**

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# Introduction

**In just 16 years Gibraltar has drawn upon its reputation as a well regulated and tax competitive commercial environment to create an archetypal on-shore licensing jurisdiction for its eGaming community.**

By placing a continuing emphasis upon licensing only the best, most committed and most consumer conscious operators, Gibraltar is now home to 25 internationally renowned remote gaming companies. Today, they account for more than 20 per cent of its GDP and represent almost 60 per cent of the UK's remote gambling presence in Europe, with more to come.

On the 11th April, 2013 at the Caleta Hotel, the third KPMG eGaming Summit drew upon Gibraltar's renown as a centre of global eGaming by once again providing a forum within which key stakeholders could gather together to discuss the present and future status of the sector.

The Hon. Gilbert Licudi QC, Minister for Education, Financial Services,

Gaming, Telecommunications and Justice kindly opened the Summit with a welcome address, which outlined Gibraltar's commitment to ensuring the safety, transparency and responsiveness of the jurisdiction in the face of challenging times for this dynamic industry. Following a regulatory update by Gibraltar's Head of Gambling Regulation, Phill Brear, the morning's sessions then continued to focus upon legislative and licensing issues, with a particular focus upon the likely impact of social gaming. Highlights included an international delegation of representatives from DLA Piper as well as a spirited address by Kevin de Haan QC on the prospect of a cohesive pan-European regulatory regime. KPMG's Archie Watt then opened the afternoon session with an address which commended the solidarity of the domestic eGaming sector in preparing for the challenges that lay ahead. Mr Watt then introduced the afternoon session as focusing predominantly upon issues pertinent to the wider eGaming industry, including payment solutions, economic development, and the 4th Money Laundering Directive. KPMG's

Sue Rossiter and the Remote Gambling Association's Simon Trussler also provided a fascinating presentation on the potential pitfalls to both governments and operators arising from implementing a new tax structure for online gaming. The Summit closed with a 'heavyweight' final panel session, moderated by Peter Montegriffo of Hassans, on the outlook for eGaming.

This report seeks to summarise the day's events with a view to capturing the expertise and enthusiasm present throughout the 2013 Summit. KPMG would like to take this opportunity to once again thank the speakers and delegates who attended, all of whom contributed to its great success. We look forward to seeing you all next year.

KPMG employs a number of eGaming industry specialists both in Gibraltar and globally and is committed to cutting through the complexity of this constantly evolving industry.

## A word from the Sponsor

**Uniquely housed 500 metres within the Rock of Gibraltar itself, our Gibraltar Data Centre reflects what we believe is the sense of security, permanence and innovation pervasive throughout Gibraltar's entire eGaming sector.**

The jurisdiction plays a significant part in our Global Private Network and represents a compelling choice for companies wishing to become part of one of the world's most sophisticated and socially engaged eGaming communities.

Continent 8 Technologies provides award winning co-location, networking, cyber security and managed services to the online gaming industry. Our sponsorship reflects our commitment



to remaining at the forefront of this exciting and dynamic industry.

Continent 8 was proud to be a part of the day's events and we look forward to next year's KPMG eGaming Summit in Gibraltar.

**Richard Ebbutt**  
**Continent 8 Technologies**

# Conference Opening

## The Hon Gilbert Licudi QC

Minister  
Gibraltar Government



The Hon Gilbert Licudi QC

**The Hon Gilbert Licudi QC is Gibraltar's Minister for Education, Financial Services, Gaming, Telecommunications and Justice. He welcomed delegates and provided a quick summary of the importance of the eGaming sector.**

In the midst of challenging times for licensees and in response to which Gibraltar (under the auspices of its Betting and Gaming Association) intends to mount a challenge to the UK's proposed point of consumption tax under EU Law, Minister Licudi opened the 2013 KPMG eGaming Summit with a spirited address.

"This is an event which is clearly and firmly established in our yearly calendar," he began. "It is, of course, no secret that Gibraltar is a world leader in online gambling. The reputation, the quality and the standing of our operators is absolutely first class, and our operators deserve to be congratulated for the responsible manner in which they undertake their business. That has been one of the key factors that have helped shape Gibraltar into a jurisdiction that is the envy of many around the world."

Minister Licudi continued in confirming that Gibraltar has become a jurisdiction that others look to and seek to learn from, particularly with respect to the

regulatory standards that it enjoys as a licensing jurisdiction. He acknowledged the work and success of Gambling Commissioner Phill Brear and his team of regulators for the relationship and the rapport they have built up with the industry, and the efforts made in striking the difficult balance between protecting the interests of customers and allowing operators to go about their business.

Drawing upon comments made during his opening address at the 2012 KPMG eGaming Summit in Gibraltar, Minister Licudi then reiterated the Gibraltar Government's commitment to licensing only the best operators in the world. "That has been the cornerstone of the Government's remote gaming policy," he confirmed. "That is still the position today, and that is a policy that will continue in the future. It is, in fact, that cautious and selective approach that has seen expressions of interest by very well known brand names and which has resulted in several new licences being granted last year. Indeed, it is my expectation that several further licences will be granted over the course of this year for operators that are considered fit to join the selection of incumbent licensees, of which Gibraltar is justly proud."

"As we all know, this is an industry that is dynamic and ever-changing"

Minister Licudi continued, "and I've always said that, despite our position, there is never any room for complacency. There is no question, therefore, of Gibraltar ever being able to say 'we've done it, we achieved our place at the head table of global eGaming'. You don't need me to tell you that in this industry, no-one in the private sector, and certainly no Government, can ever relax."

Minister Licudi explained that challenges to the industry are ever present, whether in the form of jurisdictional competition, legislative change, or the proposed introduction of taxation. "But there will, of course, be other challenges," he continued. "It is clearly the case that the EU poses a challenge to all of us, and it is a challenge that we are already confronting. You will have heard of the Government's attendance in Brussels just a few weeks ago, with the Chief Minister's speech specifically concerning gaming and calling precisely for that coherent EU policy. We demanded the right, because it is a right, for operators to demand unhindered access to the whole of the single market. Whatever the challenges may be in this industry, there will always be new opportunities that present themselves. We are certainly hopeful and we expect that the EU challenge will become an EU

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opportunity, with access to greater, more liberalised and, indeed, properly regulated markets.”

Looking further afield, Minister Licudi noted that new opportunities are already materialising in areas such as the United States, with limited intrastate gambling now being allowed in states such as Nevada and New Jersey. “And -Gibraltar operators are already taking advantage of those opportunities,” Minister Licudi confirmed. “Now there is talk of agreements between the US and other jurisdictions to create a global market of gambling jurisdictions. Those are the opportunities that Gibraltar must be first in line to explore and exploit.”

He continued, “last year at the Summit we had representatives of HM Treasury and HM Revenue and Customs, who were here to explain the UK Government’s take on the supposed need for the point of consumption tax. And it is actually good to have such representatives here in Gibraltar so that they are left in absolutely no doubt of the strength of feeling in opposition to that tax. And they should also be left in no doubt of one particular point; this is not an emotive reaction simply to greater taxation. This is an opposition based on well reasoned arguments on the

flawed basis of this proposed tax. Let me assure the industry of the Gibraltar Government’s resolve and of its commitment to continue to support our operators in whatever way we can, to continue to lobby, to continue to advance arguments in every available forum as we have already been doing.”

Minister Licudi explained that he had already discussed this issue with three UK ministers on this issue while Gibraltar’s Chief Minister had also raised the issue with UK Prime Minister, David Cameron and has made submissions to the select committee on Culture, Media and Sport. “And those efforts will continue, because the game is on and the battle has not yet been won. Whatever happens, there is one thing of which I am absolutely certain, that Gibraltar will continue to lead the way in remote gambling and Gibraltar will continue to be that shining beacon at which the whole world will look and seek to emulate. We have already earned that pre-eminent position and the Government will continue to work with the industry to make absolutely certain that we keep it that way.”

# The Regulator's Update and Perspective on Social Gaming

## Phill Brear

Gambling Commissioner  
Gibraltar Government

Phill Brear was appointed as Head of Gambling Regulation for Gibraltar in October 2007 following two years as Director of Operations with the British Gambling Commission.

In July 2011, he was appointed as Gibraltar's Gambling Commissioner in addition to his existing responsibilities. Having played a leading part in the roll-out of the UK Gambling Act and gained experience across the breadth of the British gambling industry, the switch to Gibraltar, 'home to the world's leading online gambling operators', brought a new set of challenges, with Gibraltar's adoption of its new Gambling Act. Since his appointment Phill has steered through a series of changes to the regulatory regime whilst working closely with operators and their representatives on a wide range of operational and organisational issues. Phill is also responsible for liaising with bodies as challenging as US regulators and the European Commission.

Now a regular and popular speaker at Gibraltar's KPMG eGaming Summit, Mr Brear introduced his presentation as an annual regulatory review which provides a privileged overview of events from the perspective of the Gambling Division and how they may or do impact domestic arrangements for licensees and peripheral industries. Mr Brear also expressed his intention to cover additional issues pertinent to today's industry, most notably the regulatory ramifications of social gaming.

### Licensing

Turning first to licensing, Mr Brear confirmed to the Summit that interest in Gibraltar licenses is growing at a rate never before experienced. "Surprisingly," he remarked, "we have completed only four new additions this year, but that still equates to a 20 per cent increase. One was the

reconfiguration of the Gala Coral Group, we also opened the Bally Technologies offices, likewise with Shuffle Master, and finally the introduction of Amaya through their acquisition of Ogame. Each is very different and each is underpinned by a commitment to Gibraltar's values."

"At the same time," he continued, "we have no fewer than ten companies in different stages of discussions for licensing. Some of these may not complete, although I suspect that around half will over the next 12 months and I expect that, by this time next year, we'll have at least 30 B2B and B2C licences – all readily, if not instantly, recognisable names in the remote gambling landscape."

Mr Brear explained that each licensee creates a varying amount of work for the Gambling Division throughout the year and that, overall, it is the secondary activity of licence renewals that creates the most as Gibraltar draws more and more into the approvals process each year. As such, he emphasised that the Gambling Division does need to assert regulatory pressure on partner companies. "We hope it's no more than a light and unambiguous touch," he explained, "but it is increasingly necessary as industry supply options and products multiply. We have a strong evidence base now to prove that, such is the diversity of supply, we need to do more in order to ensure the standards of those suppliers. I would like to thank those who work with my colleagues on licensing for your patience and efficiency."

### Customer Complaints

"With around twenty B2B licences, we now service in the region of 10 million registered customers in Gibraltar," Mr Brear enthused. "But the customer complaint rate remains fairly constant, with only three or four

"We have no fewer than ten companies in different stages of discussions for licensing"

## Phill Brear

Gambling Commissioner  
Gibraltar Government



contacts each week, boiling down to one or two complaint forms each month. Out of around 200 complaints each year, the vast majority are of no substance and are quickly withdrawn – frustrated attempts to cheat etc. But some do require more extensive investigation, and to establish whether the customer has been treated fairly and properly remains our priority.”

Mr Brear then explained that all investigations are conducted in meticulous detail to ensure that all conceivable ‘trapdoors’ between the Gambling Commission and the truth are closed and secured. By definition these investigations are inevitably international, occur frequently throughout the EU, although less frequently in the UK, and whilst a high proportion are from troubled gamblers who have made an error of judgement, a small proportion are customers on the receiving end of errors from operator staff or weaknesses in IT systems.

“Within that there remains a troublesome and constant trickle of high value and, at times, very sophisticated attempts to subvert the industry’s security control systems”, Mr Brear warned delegates. “Some of these cases are worth millions. And together, from the weaknesses, failures or misjudgements of some customers, through to organised attempts to extort money, they illustrate the breadth and depth of the customer base and the need for the industry to remain vigilant and continue to invest equally in customer services, customer protection and systems security. Moreover, they demonstrate the need for operators to better attempt to communicate with each other in order to deny any attempts to cheat.”

Mr Brear then went on to explain that he continues to receive a steady stream of SARs, or suspicious activity reports, copied to the Gambling Division and the Gibraltar Financial Intelligence Unit. “A significant proportion of these are leading to police interventions across the world”, he reassured the Summit. “Many are found to be unusual activity reports, rather than suspicious activity reports. Likewise the consolidated reporting

system provides a less steady stream of incidents of less consistent value. That is a good measure of both the small volume and value of fraud in the industry as well as the industry’s commitment to bear down on it at a time when many others would have you believe the issue is endemic.”

## Europe

“At the European level it is, of course, almost two years since the Green Paper (the European Commission’s ‘Green Paper On Online Gambling in the Internal Market’) was introduced, and six months since the action plan was announced”, Mr Brear observed. He went on to explain that just two weeks prior to the Summit, a draft European Parliament Internal Market Commission report emerged which endorsed an action plan that reflects the Green Paper. “So whilst the lack of travel is frustrating, there is movement, and no one should underestimate the antipathy within the EU political bureaucracy towards that movement. For many people, no progress is the preferred option.”

On a similar note, Mr Brear noted what he described as the ‘elephant in the room’ with regards to the UK’s licensing and point of consumption tax model. “The saga drags on”, he remarked, “seemingly to culminate in December of next year. When the concept of universal UK licensing was first declared in 2010, it was pretty clear that no heed of reliable evidence was going to be taken, only that which was most convenient. It is safe to say that legal certainty can be an elusive concept.”

Putting to one side the evidence base of and contentious legal issues surrounding the Gambling (Licensing and Advertising) Bill, Mr Brear explained that public policy issues have yet to be picked up by politicians, pressure groups, and the media. “It may undergo the scrutiny of parliament if and when the bill emerges, but somehow I doubt it will get the attention it deserves. The reality is that it is a side issue for government and it is a side issue for the media”, he warned delegates.

“The point I want to make about the Bill is that it is self-evidently amending legislation, therefore it is what it adds to and takes away from the 2005 Gambling Act which requires illumination and examination.” Mr Brear remarked that from a political, public policy and regulatory perspective it is a ‘clever bill’ which is as far reaching as the very act it seeks to amend, in terms of changing the face, volume and regulation of remote gambling in the UK, Europe and the rest of the world. “The bill rewrites the rule book on remote gambling”, he observed, “but not in a way that offers benefits to consumers, governments, or the established and regulated industry. Rather, it has the means and potential to ensure that everybody currently in the system loses out.”

“In my view, the bill creates ‘brass plate Britain’ for the remote gambling industry. It commits the UK to being a remote gambling licensing hub, and I emphasise here licensing, for little else will need to be there – no equipment, very few staff, and no real functionality – that’s the new model.” Mr Brear explained that as a result of the proposed amendments, the UK will offer itself as a licensing hub to Europe and almost anywhere else in the world, with all the benefits that simply issuing licences brings. “And whilst that may seem to be attractive to those who don’t understand how this industry works, even those attractions are not likely to materialise or be sustained”, he warned.

“This fundamental change in direction has enjoyed no visible communication or debate by those responsible for its rectification, there’s no reference to it anywhere. Indeed, much of it was actually invisible until the bill and the minister’s commentary on it were published in late 2012. Since then, attention has focused upon the defective process, the lack of evidence and the potential legal challenges.”

## The White List

Turning briefly to the related topic of the UK’s White List which, when introduced as part of Section 331 of the Gambling Act 2005, forbade all territories and jurisdictions located outside the EEA, UK and Gibraltar to advertise gambling products in the UK,



Mr Brear noted that the Gambling (Licensing and Advertising) Bill also “scraps that”. “Now I am not an advocate of the White List”, he remarked, “it was poorly established, it has been poorly administered, and poorly managed. The White List has encouraged a race to the bottom in terms of the reality and the application of regulatory controls. It was the UK regulators’ first foray into international remote gambling regulation and it has failed to deliver to the UK public what the Gambling Act 2005 promised – allowing instead elements of criminal behaviour, an abandonment of due diligence and the misappropriation of customer funds on an industrial scale.”

“The White List is broken”, he continued, “it has been suspended for three years. But the outcome of this blurring is the scrapping of the concept of jurisdictional approval on the basis that the UK regulator can do a better job than the white listed regulators. Instead, companies will be based thousands of miles away where that regulator has no presence or relationship whatsoever. Put quite simply, the bill proposes licensing and regulation which in practice will be conducted at massive arm’s length.”

Mr Brear explained that there is little doubt that this provision is designed to permit respected and established US operators to obtain UK licences whilst maintaining the weight of their operations in the US. However, he expressed his concern that other operators in other jurisdictions will abuse that model. “The UK already has over 3,000 licence holders”, he observed, “it does not have the mechanism or the resources to keep track of them all, over extended distances or even within the UK. The UK bill stands to dilute and further taint the supply base in the UK. It will increase costs, depress margins, and force efficiencies of outsourcing and relocation outside of the UK to a much greater extent than at present. HMRC may gain two or three hundred million in POCT, but it loses far greater amounts in corporation and employment tax. Indeed, those that survive will have even greater incentives to re-domicile themselves into more tax friendly jurisdictions.”

## Social Gaming

While just two years ago many were discussing the potential of social media as a resource for eGaming, few, as Mr Brear observed, considered social gaming as part of their agendas. “This, however, is now a conference subject in its own right”, he enthused. “At the moment we have confusion - with references to freegaming, social gaming and free betting – usually without the target of those discussions being agreed. This is not helpful to the public or the regulated gambling industry.”

“Social gaming is at a much earlier and faster stage of evolution. In the last six months, supposedly the three biggest launches of social gaming have all involved companies in Gibraltar – Gamesys with Friendzy, 888 with BingoHappy and Bwin. Party with ZyngaPlus. But of course these are not social gaming: these are licensed and regulated gambling, accessible and marketed through social media channels.” Mr Brear explained that regulators’ interest lies in whether or not these advertising channels are open to abuse by the public, suppliers, affiliates, associates or the carrier, thereby widening the scale of underage problem gambling or other negative issues.

“So my first and strongest observation, and the one that has dominated discussions with our operators, is that the marketing controls applied to the customer base have to be carried out as neatly and as tightly as is feasible. They have to be smart because without them you’re almost certainly setting yourself up for a media and maybe a regulatory fall.”

“My second point is where the game and presentation is not licensed and regulated gambling, but is gambling themed and involves payment to play – where a paid for activity offers the chance of winning a non-monetisable prize. Again, free and practice play gaming have their own issues, but the freemium model of obtaining payment to gain plays, awards, status symbols, game levels, or other features, is nudging ever nearer to a dividing line between gambling and non-gambling

entertainment. My concern here is that some non-regulated suppliers see no risk in testing where that boundary lies and, in the absence of regulatory intervention, may move products and players over the line.”

Mr Brear then warned the Summit of the growing social betting market, explaining that, generally, these are established by un-regulatable suppliers which are deemed to provide services that are not gambling. “But they are encouraging and providing the facility to loosely registered customers to bet amongst themselves on events which include professionally informed fixed odds and betting exchange type bets. So the player base of such sites is an obviously fertile ground for recruiting new real betting customers. Again, we would advise a very high degree of caution to every licensed operator stepping into these waters.”

In closing, Mr Brear remarked on growing concerns over the use of social gaming platforms to create customer databases in countries in which the operator has no existing presence. “At one level, this is an entirely legal practice in that it is not gambling. However, within those target markets the practice may well be seen in a different light; I’m already hearing noises within the EU that such activities, simply because of their potential to engage with the licensable gambling population, are unwelcome. So I would like to emphasise that wishing social gambling was a politically neutral commercial activity will not make it one. It has to be very carefully managed by the regulated industry.”

# Morning Panel Session: The Evolution of Remote Gambling Regulation

## Moderated by:

Stephen Ketteley - Partner, DLA Piper

Albert Agustinoy - DLA Piper, Madrid

Giulio Coraggio - DLA Piper, Milan

Patrick Schwarzbart - DLA Piper, Munich

**By way of introduction, Mr Ketteley explained that the purpose of the morning's panel was to explore the differences in regulation between a number of key markets and to draw a comparison between jurisdictions which are all currently at different stages of regulation.**

He noted that Italy, Spain and the UK are currently regulated while Germany, at the time of writing, is in the process of regulating. "It's an ever moving evolution," Mr Ketteley remarked, "and that's something we want to try to draw out today."

"By 2005/06 there were a handful of places that were largely regulating online gambling," he continued. "They were jurisdictions which saw the need to house and give a home to a growing industry and Gibraltar took the lead in formulating a regulatory regime which has become, as we all know, a world leader in the market. But as time went by we saw a number of challenges at European level as a very lucrative private sector and a protectionist public sector came head-to-head in a number of member states. That, coupled with the challenging economic times that we're all facing, has led to a number of jurisdictions embracing regulation. But these regulatory regimes are all inconsistent, and that's the problem."

Mr Ketteley then went on to note that each jurisdiction represented at the panel was culturally very different and that this informed the position of gambling in each respective society. This in turn frames regulation within each jurisdiction and the ways in which it may develop in the future. Drawing upon this observation, therefore, Mr Ketteley asked each panellist to first elaborate upon the ways in which regulation was driven by cultural attitudes towards gambling in their home jurisdictions.

**Albert Agustinoy:** Mr Agustinoy explained that gambling in Spain has traditionally been a secondary concern. Ten years ago, gambling as a pursuit was considered old fashioned and regulation was consequently limited due to its being almost wholly controlled by what he termed a 'state monopoly'. "So if you wanted to gamble you had the lottery, football pools, and some casinos, which certainly did not attract a growing audience at all. This approach changed, however, with the introduction of online gaming, the introduction of new gaming platforms and also a new environment that clearly connected with a new audience."

Mr Agustinoy then went on to explain that this has resulted in a change in the perception of online gambling. The sports betting market has changed and grown very popular among the mass

Spanish audience while online poker now attracts many more sophisticated users such as university students and young professionals. "So gambling has become a very popular pastime due to its increased availability and diversity, although it should be noted that 80 per cent of the market is still controlled by the state monopoly so we have a long way to go."

**In stark contrast to what could be considered a relatively permissive Spanish regime, the German regime appears to be very protectionist. Is this fair to say?**

**Patrick Schwarzbart:** "It is very protectionist," Mr Schwarzbart agreed. "In Germany we also have a very traditional background in gaming but this concerns specific types. For example we have a very strong tradition of horse-race betting, a sector which has been regulated for over a hundred years and is also open to private operators, while we also have a very strong sector for gaming machine operators. But I think the intention of the regulator has been to protect the position of the lotteries to a large extent and that can clearly be seen as protectionism."

Mr Schwarzbart explained that Germany had made good progress concerning the regulation of gaming types such as poker and could at one point have been considered liberal in

“I find it very interesting that the regulator is not now adapting to new market offerings, to the interests of the market, or to the interests of the player.”



its approach. However, he also noted: “I find it very interesting that the regulator is not now adapting to new market offerings, to the interests of the market, or to the interests of the player. The stark contrast between Spain and Germany is that whereas in Spain gaming is seen as part of the entertainment industry, I always get the feeling that the German regulator considers gaming as something that players need to be protected from. Somehow remote gambling is seen as a threat by regulators, to the state lotteries and also to the players.”

**Italy as a regulated market also appears to be embracing online gaming rather than trying to protect any other interests in the market, is this true?**

**Giulio Coraggio:** “I think it’s interesting to note the comments made about the old fashioned gambling industry;” Mr Coraggio began. “My contention is that gambling in Spain was not old fashioned, part of it was just unregulated, so the Spanish were already playing on unlicensed platforms and now do the same on licensed. The regulators simply provided a more secure environment for players. In Italy we too tried to regulate although it took time because regulators were not at first sure how to accommodate the needs of players.”

“There is also a general understanding in Italy that the only way to fight against unlicensed operators is to keep taxation low. Low taxation is a great way to compel operators to work in a secure environment. Throughout the rest of Europe, however, there is still a lot of very negative publicity surrounding online gaming and gambling in general. A lot of this is, of course, due to misinformation and I do understand that regulators are getting more knowledgeable about how the sector works, about the need to protect players, to bring them into a safe environment and to make regulations more suitable for operators.”

**Do you think Italy is succeeding in allowing the industry to flourish while protecting the player? Do you think that balance is right or wrong?**

**Albert Agustinoy:** Mr Agustinoy agreed with Mr Coraggio on the fact that, if there is a demand for gaming, an online environment is either regulated properly or becomes a black market environment. “In Spain we have a good departure in that regulators are able to operate within a fully regulated market and we have found that while the black market has been reasonably low, in the case of online slots or other types of games that have not been regulated the degree of black market incidents remains quite high.”

Mr Agustinoy explained that simply by using a VPN [Virtual Private Network], or similar online tool, any Spanish user can gain access to these types of unregulated games. “So I wholly agree that regulation must certainly ensure a degree of protection and at the end of the day this is a win-win situation for everyone – the player gains a well-protected system, the operators have the insurance that they know the rules of the game, and the whole industry becomes more reliable and is therefore more trusted as a form of entertainment.”

**What is the relationship like between the regulators, the legislators and the industry in as far as educating your regulators as to what they need to consider?**

**Giulio Coraggio:** Mr Coraggio began by noting an interesting comparison made last year which showed that the illegal gaming market in the Italian casino sector was almost €10 billion more profitable than the legal market simply because slots were not legal. The regulator responded that it was largely powerless as a result but urged licensed operators to point out which organisations were operating illegally. “Regulation in that respect has since improved, so operators must work with the regulators for a better environment. This is proof that the lobbying can work from both sides.”

**Albert Agustinoy:** Mr Agustinoy added that, from his experience, a key strategy for building relationships with regulators lies in explaining the industry to them from an operator's perspective. "It may seem obvious, but detailing the particulars of games and the ways in which the industry operates can greatly facilitate licensee/regulator relations," he remarked. "We must let them know of the more reasonable solutions for operators and the ways in which they can be applied. This is a key factor in evangelising the industry because we often find ourselves in challenging situations simply because of a lack of mutual understanding."

**Germany is obviously the hot topic of the moment. What is the current situation with the evolving regime there?**

**Patrick Schwarzbart:** Mr Schwarzbart explained that there is still a lot of movement with regards to regulatory development in Germany but expressed his desire to first step back and address the issue of dialogue within the domestic German industry. "We had this short window of opportunity in Germany not too long ago and the regulators there had a very open ear for the industry," he noted. "They were very interested in regulating the market and within that period of just eighteen months almost fifty licences were issued. In other regulatory areas, however, specifically those responsible for issuing and monitoring sports betting licences, we had a very different experience. Talking to regulators we felt that licensing and regulation was just a task to get over and done with, and I came away with the impression that they don't really want to regulate the market. So I think it's now a very difficult situation with respect to a dialogue between those two parties."

With respect to taxation, Mr Schwarzbart then observed that operators have always argued against a turnover-based tax. Nevertheless, the German federal legislator decided to

introduce such a tax on sports betting and on a point of consumption basis which, he noted, imposes some difficulties for operators to provide competitive betting in Germany. "So, again, there is a question mark behind that tax," Mr Schwarzbart remarked. "Was it really introduced to regulate the market or rather to protect the incumbents? Is the true intention of that tax not to have remote operators struggle to provide competitive terms? Currently, the state monopoly has been suspended and there is the opportunity for up to twenty licences to be issued for sports betting. This process has been going on since August, 2012 and we are now in the final stages of invitation and concept presentation. The regulator will soon come to a decision as to which operators will receive a licence and, since the European tender, there may be an opportunity to appeal these decisions. But those 130 out of 150 applicants that do not receive a licence will probably face the same problems as they have in the past: will they still risk enforcement actions to offer their products in the German market?"

**What is the current situation with the unregulated market in Spain? What can we do about it?**

**Albert Agustinoy:** "I think that the regulated market is something of a private club," remarked Mr Agustinoy, who explained that, under Spanish law, the operation of non-licensed gaming activity may still result in extensive sanctions. "The regulator has been in very direct contact with payment processors, internet services providers and others in order to cut the black market supply as quickly as possible. I'm aware of ISPs already being provided with a number of IP addresses to be blocked, which is far from a complete solution, but there has been some significant counter action even to block aspects such as the payment of prizes. So there is a black market but that still remains quite low."

**A number of people are talking about the use of black lists for operators which, I understand, Italy has had for some time. Has that been successful?**

**Giulio Coraggio:** Mr Coraggio expressed his concern that the use of black lists to assist regulators in blocking domain names is thwarted by many unlicensed operators changing their domain names on an almost daily basis. "It is not IP address blocking so it's very easy to bypass. Even some of the other measures put in place are not being enforced at the moment and if the solution does not come from the industry then it is unlikely that the solution will be effective."

**Lots of jurisdictions have very different views on how to regulate the social gaming aspect of the industry: could you elaborate upon your respective experiences of this?**

**Giulio Coraggio:** Mr Coraggio explained that the problem lies in the blurring of the boundaries between traditionally licensed remote gaming activities and increasingly diverse social gaming formats. Moreover, he explained, gambling is still defined in a parliamentary act making it difficult to include social gaming within what is now an accepted definition of gambling.

**Of course skilled gaming is regulated in certain ways and many social games would, in most cases, not necessarily be considered skilled.**

**Giulio Coraggio:** "Skilled gaming is regulated in the case of prizes in kind or prizes in cash. When there is no prize there is no regulation, however. So the question is, if the gambling regulator does not regulate the sector, does it fall under consumer protection? These are the issues that need to be addressed if we are to ensure adequate customer protection through regulation."

# A Coherent EU Policy on Cross-Border Remote Gambling Issues - The Impossible Dream?

Kevin de Haan QC

An internationally acknowledged expert in all aspects of e-commerce regulation, Kevin de Haan QC is a specialist in Consumer Protection and Gambling Law, particularly where an element of Public International or EU Law is involved. Having led the team that drafted the Gibraltar Gambling Act, Kevin has been closely involved in the development of the online gambling industry since its inception in the 1990s and is recommended as a leading Silk in four practice areas by The Legal 500 and Chambers and Partners Directory.

A highly regarded and impassioned speaker, Mr de Haan opened his presentation by congratulating the previous panellists for highlighting the difficulties of attempting to reach a consensus about regulation on a pan-European basis. "We have very, very different systems internationally," he explained, "and the speakers highlighted one major problem, which is that of definition." Mr de Haan observed that the UK has historically regulated gambling according to the definitions of what he described as different gambling 'products' – betting, gaming, lotteries, and skill based games. In other jurisdictions, however, definitions are completely different. In Germany, for example, Mr de Haan identified considerable overlap between what the UK would conceive of as skilled betting and gaming, with the German concept of games of chance. "So what I'm trying to say is

we are all speaking a different language in terms of the products that we are dealing with."

"So what I want to try to do is look at how we could possibly move towards a pan-European system of regulation because that must be the ultimate goal," he continued. "If you look at the notion of harmonisation within the EU – the creation of a level playing field within a single market where everyone abides by the same rules and no one is given a competitive advantage over another – how can that be achieved with the gambling market?"

## A Brief History

Mr de Haan observed that remote gambling in particular is at issue because it is the only form of gambling that crosses land frontiers and raises cross-border issues. He then explained, however, that "we cannot look at how to arrive at a consensus without first exploring the history of regulation." Drawing upon Britain's history of land-based gambling in particular, Mr de Haan noted that the domestic gambling industry was at one point almost entirely in the hands of 'the mob': "every east-end gangster wanted to have a stake in one of the many illegal gambling clubs around London and so, on the back of a Royal Commission, the decision was taken to bring gambling into the regulated fold. For the first time, therefore, we had the possibility of having the creation of betting offices, the first

legal casinos in the UK, and we had a greater number of society lotteries under the gambling legislation of the 1960s."

Still in its embryonic stages of legislation, however, this system retained a 'trial and error' approach. In the absence of a gambling commission, regulation was in the hands of the police and the magistrate, meaning that there was no mechanism in place either to protect the public or to promote gambling, which was still regarded as a social evil permitted simply because of the existence of an unregulated market. "The '60s legislation was a partial success," Mr de Haan noted, "but the problem was it led to an explosion of casinos in London and those again fell into the hands of organised crime. So, by the late 1960s, there was real public concern about the regulation of gambling in the UK."

As a result, in 1968 the UK Government enacted the Gambling Act, which eventually created the Gambling Board. Over several decades, as Mr de Haan explained, the UK's gambling industry was subsequently and gradually brought into order; the industry developed and the UK arrived at a situation, by the time the Budd Report was published, gambling was entrusted to a vibrant private sector subject to careful regulation by the Gaming Board in its areas of competence.



## A Change in Attitudes

"We saw, on the back of that, a sea change in public attitudes towards gambling," Mr de Haan enthused. "Gambling was originally regarded as a social evil, something to be avoided and suppressed. But Budd [Sir Alan Peter Budd, GBE, a prominent British economist] looked at the social scene and realised that the public were now beginning to regard gambling as a part of the leisure industry. The biggest sea change that affected these attitudes was the shift in regulation. Previously the regulator's sponsoring department was the Home Office but this then came under the DCMS, or the Department of Culture, Media and Sport. It probably, however, best belongs now under the control of those government departments that deal with the regulation of business, because the one thing that the European Court has recognised is that the provision of gambling services is the provision of financial services – and that is precisely what they are."

## The UK

"In the UK, we now have a regulator which is responsible for regulating the whole of the gambling industry – not just gaming but also lotteries, prize competitions and products of that nature," he continued. "But we have a situation in the UK now where a great deal of the expertise on the Gaming Board was lost, largely due to the way in which it was set up. The Gaming Board was originally established in London but was later moved to Birmingham, meaning that a large body of staff already set up in London was asked to move 120 miles away. I'm not saying that there isn't still a great deal of expertise in the Gambling Commission, only that a lot of the original expertise and experience that the Gaming Board brought to the table was lost."

## Jurisprudence

Mr de Haan continued in expressing his suspicions that the UK Government's proposal for a dual licensing system is driven, in truth, by taxation. "I suspect that the DCMS was handed a document saying 'we need to raise £X billion from the online gambling industry, how do we do it? – and that's a very difficult brief. So let's head back to the jurisprudence of the Court of Justice of the European Communities [CJEC]."

Most cases that appear before the CJEC, as Mr de Haan described, start in the national courts of the Member States. The Member State introduces a measure which is restrictive of freedom of establishment or freedom to provide services, among others. An operator or commercial enterprise therefore complains to the national court arguing that the national measure is inconsistent with the provisions of the relevant EU Treaty. It then falls to the national court to interpret EU law. The national court can interpret EU law on its own basis i.e. give its own interpretation, but where it needs assistance there is a procedure where the matter can be referred to the European Court of Justice in Luxembourg for a preliminary ruling on the meaning of the relevant provision of EU law. The Court of Justice may not rule on whether the national measure is compatible with EU law but it does on occasions give very strong direction to the national court on whether the measure is compliant with the provisions of the treaty."

## European Court Rulings

"Now what we've seen to date is a series of peaks and troughs in the European Court," Mr de Haan observed. "If you start out with Schindler, which is the very early case

on lotteries and which established that gambling was a financial service, the court there said that because of the curious nature of lotteries a large margin of appreciation has to be given to Member States in what measures they introduce to regulate gambling and what degree of penetration of the national market they allow to operators established in other Member States – and Schindler was really a restrictive decision. But we later moved on from Schindler to cases such as Gambelli and were virtually looking at a passporting of licences throughout Europe – things looked very bright."

"But then, of course, we come down to Santa Casa da Misericórdia, the case concerning Portuguese gambling monopoly, which is greatly embedded in Portuguese culture," he continued. "I don't think Santa Casa really set any great precedents – it was a case very much based on its own facts – but if you then move on to the more recent decisions in Stoss and particularly the very important HIT and HIT LARIX case on land-based gambling, I think we're seeing a move back towards a more open and less restrictive approach and the giving of a smaller margin of appreciation to Member States."

## Evolution

"One of the great things to emerge from the Stoss decision in particular is that it has highlighted a lot of hypocrisy in the way that gambling is regulated. If you have a system whereby your Member State gives over the provision of gambling services to a state monopoly or a state sponsored monopoly, yet you rely on that monopoly to aggressively promote its services to members of the public, you cannot then complain that if you allow other operators in other licensing states to come in they might pose a threat or danger to vulnerable people."

**“The future lies in mutual respect and mutual recognition of the regulatory systems that exist within the European Union at the moment.”**

Mr de Haan then warned the Summit that a key problem with the European Court remains its lack of understanding of the online gambling industry. Although as a sector it has generated more cases than any other form of commercial activity within the European community, an understanding is only now being formed. “I think now the penny is slowly beginning to drop in Europe and I think that one sees that in the HIT and HITLARIX case,” he remarked.

“It makes very interesting reading if you are interested in seeing how the approach of the European Court of Justice has evolved over, effectively, two decades. If you read that you’ll see that Advocate General Mazak is saying ‘yes, you can introduce restrictive measures but those measures have got to be proportionate’. In other words, first of all they must be no more restrictive than is absolutely necessary and they must be effective for the realisation of their policy objective. If a Member State seeks to justify the introduction of a restrictive measure to deal with a particular problem, say the prevention of gambling addiction or fraud, it must produce evidence of the existence and extent of that problem before the national court – because it is the national court that decides the facts. That is why I think the UK’s case for dual regulation will fall down, because the evidence is just not there.”

## **Evidence**

Ultimately, as Mr de Haan explained, there is a distinct lack of evidence to justify the sea change in the new UK approach because the Gambling Act almost institutionalises the passporting of licenses into the UK from European jurisdictions, “so why are they changing it?”

“Well I think we all know the answer to that,” he remarked. “The change is tax driven. In a situation where the UK Treasury is very strapped for tax revenues it is looking around to see where additional revenues can come from. And if you really want to tax the industry effectively you have got to license it.”

## **Where does that take us?**

Mr de Haan observed that the UK development is almost a microcosm of the problems that any regulator in any Member State is likely to face in trying to justify the introduction of restrictive measures. “We will go on until we have some form of harmonised system in Europe,” he observed, “with a toing and froing between the Commission. But where do we start in trying to establish a regulatory regime that will work throughout Europe? It’s very difficult because of the differences in the structure of the industry and the regulatory regimes in different countries. But there are features that are common to all of them and you can always find that the goals in any regulatory system are consistent with Section 1 of the Gambling Act 2005 – keeping gambling crime free, ensuring that gambling is fair and transparent, and protecting children and vulnerable people. It ought to be possible.”

## **Where is the way forward?**

“An initial way forward might be in the creation of a European code of practise and this needs regulators to get together,” Mr de Haan emphasised in conclusion. He explained that the industry is starting to see the seeds of cooperation in, for example, a recent meeting of four regulators to try to use the procedures for enhanced cooperation in article 239 of the treaty.

“And I think in that one might see the seeds of a move towards a pan-European regulatory regime.”

“Even if a few Member states signed up to that and adopted common standards, that enhanced cooperation might, in due course, form the basis for some form of pan-European regulatory system. But my view is that we are never going to see a European Gambling Commissioner. We are never going to see a totally harmonisation directive. The future lies in mutual respect and mutual recognition of the regulatory systems that exist within the European Union at the moment. That is, I feel, the only way that we are going to move towards a coherent system and a consistent system for the regulation of online gambling within Europe.”

# Introduction to the Afternoon Session

## Archie Watt

Head of eGaming  
KPMG Gibraltar

Archie joined KPMG Gibraltar from KPMG London, where he was recruited as an IT Advisory Director in the Information, Communication and Entertainment practice, with a particular focus on online gaming clients. Archie worked on the bwin/PartyGaming merger and he has also worked on a number of acquisitions in the gaming sector and the public listings of 888, Playtech and PartyGaming, amongst others. Archie is a regular contributor to sector publications and recently co-authored the report *Online Gaming: A Gamble or a Sure Bet?*

“I’ve been involved in the eGaming sector for fourteen years now, and one of the things that I’ve come to realise over that time is that it constantly evolves.”

Having expressed his thanks for the morning’s presentations and congratulated delegates for their enthusiasm during the geographically focused session, Mr Watt introduced the afternoon’s proceedings as a sector focused examination of the wider issues operators face and how to prepare for the challenges and opportunities that lie ahead.

“The first presentation will be by Stuart Ballan of Counting House, an organisation which really ‘gets’ the sector”, Mr Watt began. “He is going to be talking about the fundamental changes in payments regulation and methodology, a very important topic because, after all, the only way for the industry to make money is by getting money on to the sites. If there is a new trend in payment methods or technology and you’re left behind the curve, your competitors will gain a significant advantage. And we all know what happens in this industry to those who get left behind.”

“Stuart is then going to be followed by Michael Tobin of Continent 8”, Mr Watt continued. “Michael has been instrumental in creating the Continent 8 brand and is a very strong supporter of the sector. With their global footprint, Continent 8 can provide hosting facilities where and when you need them and here in Gibraltar, together with GibTelecom, they can provide hosting facilities and bandwidth that is the envy of many other territories. Michael is going to impart some insight into the importance of entrepreneurship and economic development on a global scale and that surely will provide some food for thought this afternoon.”

“I’ve been involved in the eGaming sector for fourteen years now, and one of the things that I’ve come to realise over that time is that it constantly evolves. Legal and regulatory issues are constantly changing, but you are adapting, and that is the most remarkable thing of all about this sector”, he enthused. With allusion to regulatory evolutions such as FATCA, or the Foreign Account Tax Compliance Act, Mr Watt then drew the attention of the Summit to Peter Howitt’s forthcoming presentation on the 4th Money Laundering Directive. “One of the more eye-catching proposals in that draft text concerned extensions to our compliance requirements concerning PEPs, and this is just one of the things that we later hope to address.”

“After coffee we have two more presentations which I’m sure will keep you on the edge of your seats”, Mr Watt continued. “Sue Rossiter of the Remote Gambling Association and Simon Trussler of KPMG will be talking



about tax. I'm fortunate enough to have already seen the presentation that Sue and Simon will be presenting this afternoon and I can honestly say that the concept of operators being able to maximise revenue while Governments can, at the same time, maximise tax take is truly an exciting prospect."

Mr Watt then described his pride in being able to introduce what he described as a 'heavy-weight' panel session to close the day. Moderated by Peter Montegriffo of Hassans and featuring GBGA Secretary Simon Howitt of Ramparts Law, Michael Carlton, CEO of Victor Chandler International, Kevin de Haan QC and Adam Craig, group director of tax at bwin.party; together they would tackle the outlook for eGaming within the context of an increasingly fractured European regulatory framework and new opportunities in the US and China.

## Archie Watt

Head of eGaming  
KPMG Gibraltar

# Hot Issues in the Payments Industry

## Stuart Ballan

Head of Sales - Middle East  
Counting House Ltd.

**Stuart Ballan, MBA (Kellogg-Recanati) is Head of Sales for the Middle East at Counting House Ltd. He has over 25 years of business and B2B experience, including his own entrepreneurial ventures, working for a leading gaming operator, for an acquiring bank and, currently, for a leading-edge PSP with global coverage. Based in Tel Aviv, he is a keen cyclist and a published children's book author.**

Fundamental changes in payments regulation and methodology are again afoot. What are their implications for operators and professionals?

Mr. Ballan began his presentation by providing an introduction to Counting House Ltd., which provides payment processing services predominantly to the eGaming industry. Counting House is part of a group of companies that for nearly 20 years, has provided similar services to many industries, including direct marketing, publishing, eCommerce, Forex, affiliates and charitable organisations.

## War Creates Innovation

Mr. Ballan stated how "war creates innovation", giving the example that there have been more advances in aviation in two world wars, including the jet engine and the nuclear bomb, than in any twenty year period free of war.

Mr. Ballan began with an example of a more recent 'war': the Cyprus banking crisis, where Counting House created and launched an emergency package within 24 hours of the Cypriot government announcing its intention to levy all Cypriot bank deposits, as

part of a €10 billion bailout solution. "It was a very quick war", Mr. Ballan explained, "But in this case, innovation became the lifeline of companies that had lost the ability to take deposits and payments, more or less overnight."

"Similarly, there has been more progress in the financial world in the last ten years because of internet gaming than there has in the last hundred", Mr. Ballan continued. "Most of that has been driven by the eGaming sector and a lot of other industries have benefited as a result. It's critical to the success of any eGaming operation to be able to send and receive money from people using methods that are convenient to players and operators alike. And we have to do so within a growing, extremely confusing and ambiguous regulatory environment."

Such is the extent of this ambiguity, Mr. Ballan explained, that the payment processing industry has been forced to respond with a degree of creativity within a fractured regulatory environment that has in some cases resulted in non-compliance. "Some of that is good for the industry, however, and today I'm going to be talking about some of the pressing issues and their solutions."

## Anti-Money Laundering

"To begin, I was very pleased to note that my presentation on AML is consistent with this morning's observations about what's happening in Germany", he continued. "And it is in line with this theme that I'd like to discuss, not just how AML can affect where your operations are licensed today, but also how your licensing

decision of the past can dramatically affect what you can and cannot do today. There are many jurisdictions where you can license and you make decisions based on the balance sheet at the time, but things change. In Germany, for example, changes to AML guidelines combined with ambiguity have triggered real changes to payment processors which, in turn, has a material impact on operators."

Mr. Ballan explained that these changes were triggered by German legislators being reprimanded for their anti-money laundering practises in sports and casino betting. "Since then, there have been drafts and re-drafts, sections and subsections, and this serves to create even more uncertainty and ambiguity", he observed. Mr. Ballan drew upon the example of a past requirement for all players to be authenticated by face to face verification and later to submit by email, notarised verification in the form of passports and driving licenses, all of which measures were driven by regulatory ambiguity, yet were blatantly impractical.

"One of the concerns in Germany surrounded anonymous deposits and withdrawals; all the cash-type payment methods that can't be tracked the way credit cards can be, etc. The impact was that the payment providers withdrew services for non-EU licensed gaming operators within Germany. So what I want to discuss is the decision the payment providers made and why they did so."

## AML EU or Non-EU?

"If you are an EU licensed operator, it's okay to take payments using payment methods such as a PaySafeCard, Skrill

“There has been more progress in the financial world in the last ten years because of internet gaming than there has in the last hundred.”



**Stuart Ballan**

Head of Sales - Middle East  
Counting House Ltd.

and cash-type anonymous payments. But if you are a non-EU licensed operator it's not," Mr. Ballan observed. "So all EU is good, all non-EU is bad?," he continued. Drawing the attention of the Summit to a presentation slide, he then showed that Gibraltar, Cyprus and Malta are classified as EU jurisdictions, whereas the Isle of Man, Alderney, Guernsey, Costa Rica, Curacao and the British Virgin Islands are non-EU jurisdictions. "So there is a clear inconsistency in AML impact here when we consider the current banking crisis in Cyprus, (EU licensed) compared to the Isle of Man, say, which is highly regarded for its regulatory framework and increasingly so every day, yet is non-EU licensed and such payment methods were withdrawn. This is an example of how a decision made years ago can actually affect operations today."

## Germany Rationale

So why did payment processors withdraw their services from non-EU licensed operators? Mr. Ballan explained that payment providers want to be approved for future Germany gaming regulation, so the last thing they need is to be on the "wrong side" of the German regulator. "There was

minimum risk in processing for EU licensed operators, as German gambling regulation is not compliant with EU law due to provisions made for the free movement of goods. So a payment processor or an EU operator can always claim it's acting in compliance with EU law, knowing any argument to the contrary can only be addressed in court, with payment providers and operators being in a strong position to win. However, by definition, the non-EU licensed operators are outside of EU law and don't want to play with fire."

So what was the cost? Mr. Ballan explained that payment providers subsequently removed selected services from operators based in non-EU jurisdictions, resulting in companies such as Paddy Power and PKR, for example, losing some of their payment deposit capabilities. "And this was all the result of complex, ever changing and ambiguous AML guidelines influencing decisions concerning where to license made years before."

## Gaming 'vs' Financial

"Within the gaming and financial industries there is an 'identity crisis' for companies in the binary options, Forex and lottery messenger industries, that don't want to be painted with the same brush as the gaming companies," Mr. Ballan observed. "And this battle is based around the demands of the acquiring banks and the credit card schemes. It was discussed earlier that the legislators and the regulators either do not understand what these industries are, or perceive them differently, and this is a constant battle. Companies in these three industries are constantly battling to not be identified as 'gaming', because payments processed as such would suffer higher declines and geographical limitations, consistent with the gaming industry. At a detailed level, it all comes down to merchant codes."

Mr. Ballan explained that with every transaction processed via a credit card, a four digit MCC code is passed to the banks. So, when you buy your groceries at the local supermarket, the MCC code used to identify this transaction effectively tells the banks it's a purchase of perishable goods in

“Increasing ambiguity and these ever changing guidelines and rules breed creativity, however, they also breed non-compliance, and that cannot be good for the industry in the regulated market.”

the retail industry, and that the goods are unlikely to be returned, and that the consumer is unlikely to claim (s)he didn't make the transaction. “But the battle here is that the binary options and lottery messenger industries want to get acceptance from the acquiring banks and card associations, Visa and MasterCard for example, to not be processed as gaming, as firstly, many banks decline the online gaming MCC code (7995), and secondly, because such payments will probably not be processed in countries that have banned eGaming, thereby materially reducing the industry size.”

### Lottery Messenger

“I live in Israel,” explained Mr. Ballan, “and if I decide to buy a ticket for the UK lottery, I've got two choices: I can either fly to the UK myself to buy a ticket, at a cost of hundreds of pounds, or I can take advantage of a growing, global industry that allows me to go online and legally buy a ticket for the same UK lottery (and for many others), paying a small premium on the ticket price for the service.”

Drawing the attention of the Summit to the associated slide, Mr. Ballan then noted that he had chosen to typeset the words 'lottery messenger' in red and green respectively “because I think that perfectly sums up the industry – What do you see when you look at these two words? The word 'lottery' or the word 'messenger'?” Mr. Ballan explained that the companies within this industry are, in essence, couriers – they have no business relationship with the actual lotteries. “All they are doing is taking online orders and sending couriers to buy the tickets for you. So are they in the lottery or gaming business, or, like FedEx, in the courier/messenger business?”

“The problem is the banks and regulators do not understand, so they have been forcing these transactions to be processed as gaming, or 7995, rather than 4215 for freight forwarders, drastically reducing the size of the industry for the reasons I explained earlier. Let's take an example. You go into a newsagent and buy a newspaper, a chocolate bar and a lottery ticket, and you pay by credit card. In most countries this wouldn't be processed as a gaming transaction, whether you included the lottery ticket in your 'basket' or not. But when you move on to the online world of lottery messenger, suddenly the same lottery ticket purchase is classed as gaming, and processed as 7995, yet both the newsagent and the online lottery messenger companies clearly performed the same service of being a courier type channel for a lottery ticket, purchased through a valid retail outlet. This is a huge industry, that the majority of people have yet to discover, and what we're trying to do at the moment amongst all this chaos, ambiguity and confusion is to create and deliver a legal solution for processing the industry as non-gaming, thereby providing the platform to enable rapid industry growth.”

### The USA

Turning to the increasingly topical subject of gaming in the USA, Mr. Ballan noted that Nevada, Delaware, and New Jersey are imminently (at the time of the summit) expecting to legalise online poker and casino. However, these three states represent just 4 per cent of the US population, so how will the other 96% be able to pay and play? Mr. Ballan then drew the attention of the Summit to a graph depicting the share price of a well-known, public eGaming company between 4th February and 1st April 2013 and noted that, following New Jersey's announcement of its intent to legalise eGaming, the share price had

increased by 50 per cent during that period. "I saw many attendees at ICE 2013, London, celebrating the rise of their personal assets during that exhibition. But given that share prices represent future earnings, which in turn come from cash, have you stopped to think about how the future USA gaming players will actually make the deposits that will generate these earnings? It turns out, payments for US gaming remains undecided and ambiguous."

## Credit Cards in the USA

Generally speaking, as Mr. Ballan observed, 80 per cent of US non-gaming transaction are made using credit cards, "the American public is used to using credit cards, and it's not for us to try to force them to pay in different ways, that they are not comfortable with. So how will credit cards be used? Unfortunately, for operations that might be only months away, today, we still don't know."

"If you live in New York, but next week, you'll travel to Nevada, for a 'gaming weekend', do you have to wait until you arrive in Nevada to deposit funds, or can you do so from home, work, or on the train, when in New York? We don't know," Mr. Ballan stated.

"I mentioned earlier that payment processing in credit cards is driven by four-digit merchant codes, and that gaming uses 7995, which has been blocked in the USA for years. Will the US suddenly start accepting 7995 transactions? If so, only when initiated in one of the 3 licensed states, or from anywhere? How practical would it be to allow 7995? It turns out, credit cards in the US are generally issued on a national level rather than a state level – so it's not as if you can get a Nevada issue credit card to identify just Nevada players. Furthermore, even if the issuing banks said yes to 'gaming

ready' or 7995 cards, it would take years to slowly implement, as the same banks spent years blocking such transactions. Untangling the web they built would be far from simple. We also can't assume that only Nevada residents would play, or that non-Nevada residents would not bank with a Nevada bank, or that a Nevada bank would be able to trace where a payment is coming from – so it's extremely complicated."

Mr. Ballan then noted that one option is for MasterCard to allow use of its 9754 code, currently used for legal horse and dog racing, for US gaming. However, there's no decision from MasterCard.

Similarly, other deposit methods such as PayPal are still unconfirmed, while ACH, a payment method prone to fraud, is expected to be a key initial deposit method. Many alternative methods such as eWallets, pre-paid cards, PaySafeCards, Skrill and Neteller, meanwhile, still have to be registered for eGaming use in the US. "With the launch of US gaming on the near horizon, the whole subject of gaming deposits in the US is filled with uncertainty."

So, yes, the share price jumped 50% on the news of the US markets opening up soon. But clearly, there's still a lot of work to be done for the gaming operators to accept the deposits that will be the future fuel for their earnings."

## To Close

In closing, Mr Ballan drew the attention of the Summit to a slide depicting a struggling tug-of-war team. "For me, this picture sums up the gaming industry: we see many people shouting independently at one another, whilst digging their heels in – the AML organisations, the acquiring banks, card associations, regulators, compliance, operators, players, etc. The result is the pain you see on their faces, resulting from different parties pulling as hard as they can, in different directions. We, as the gaming industry, and as payment processors, need to meet the needs of all these shouters, in a world where what they are shouting about is usually muffled and constantly changing. Today, we have multiple payment methods that have appeared in response to global demand for fast, secure, guaranteed payment, in gaming, and beyond. Whereas this increasing ambiguity and these ever changing guidelines and rules breed creativity, however, they also breed non-compliance, and that cannot be good for the industry in the regulated market."

Banks fear the every changing rules; regulators are faced with constant steep learning curves and workloads; and operators want efficient payment products, yet the less the merrier, to reduce integration. The only option is to bring together these disparate parties and try to formulate less ambiguous requirements and simpler and more secure means for operators and players to process their transactions. Doing so would be better for banks, governments, players and operators"

# Entrepreneurial and Economic Development

## Michael Tobin

Co-founder and Chief Executive Officer

Continent 8 Technologies

“We have recently been consulted by and will be presenting in Delaware at the end of the month and this is because they see that we are in a position to help them to provide a platform for their state lottery licensees.”

**Michael is co-founder of Continent 8 Technologies PLC and the creator of the "Continent 8" brand. He is a Certified Public Accountant by profession and an entrepreneur by nature. He is a former Director of Empire State Development, the lead economic development agency for New York State. Michael is a graduate of Montreal's McGill University.**

A key figure in the global eGaming community and a noted speaker worldwide, Mr Tobin began his eagerly anticipated presentation by introducing delegates to the history of Continent 8 Technologies and its role within the industry. “The whole concept of Continent 8”, he explained, “evolved when my co-founder, Jay Stubina, and I were students together at McGill University many years ago. In the late 1990s we both realised that we had missed the dotcom boom and asked ourselves how we could get involved in online. So we came up with a concept based on a combined theory of the death of the nation state and the creation of supranational commercial zones and megatrends. We called it the ‘eighth continent’ or Continent 8: what we’ve become is eGaming’s multi-jurisdictional hosting solution.”

“The moves we have made have been very much based on the needs of our customers”, Mr Tobin continued. “Many different solutions have also come from our work with a lot of different jurisdictions however, so we have also become a fiduciary to regulators and advisors to governments because they see us as a neutral, objective and knowledgeable part of the e-commerce world. We have recently been consulted by and will be presenting in Delaware at the end of the month and this is because they see that we are in a position to

help them to provide a platform for their state lottery licensees. We are also working with parties in California, New Jersey, Florida and New York and, of course, we are working in locations throughout Europe with regards to expanding licenses based on the security and accessibility of infrastructure. Not everything stays the same in this industry, as Gibraltar is currently experiencing with the point of consumption tax, and we have to be entrepreneurial in order to allow economic development opportunities to take place for private business and for governments.”

“So Continent 8 allows companies to have a global, single source supplier in a complicated world both regulatory-wise and technology-wise”, Mr Tobin continued. “We host, we co-locate, we do disaster recovery, network management, positioning, and we are one of the early adopters of methods to protect clients from DDos, or Distributed Denial of Service, attacks. This again came as a result of the needs of our customers who felt they were under threat from these sorts of attacks and we said ‘let them come!’”

Mr Tobin then explained that Continent 8 currently operates from nine locations around the world although the company’s main points of presence are to be established in North America. London, Paris, New York and Dublin are each host to major data centres while Montreal is home to Continent 8’s original data location. “We headquartered, when we left Montreal for the first time, in the Isle of Man for a number of reasons and we continue to operate a data centre there”, Mr Tobin also explained. “While we look forward to making Gibraltar our ‘rock’ for a number of reasons. But a lot of our reasons to locate are predicated upon where our customers need to be and where we are invited

# Michael Tobin

Co-founder and Chief Executive Officer  
Continent 8 Technologies



to be by our regulators in order to control and manage licensee bases.”

## Gibraltar

“Here in Gibraltar we have a very niche location. We were introduced to the island a number of years ago and knew at that time that it was becoming a jurisdiction of choice for a lot of very important companies, most of which are here today,” Mr Tobin enthused. “But it has also become a very challenging location from a technical point of view.” Mr Tobin explained that Continent 8 acquired the unique location of the Ministry of Defence’s old communication centre, which is located at the heart of the rock of Gibraltar. Many had tried to initiate and develop the site but did not have the technical capabilities to realise its full potential. “We acquired the site at a time when its ownership had been transferred to the Gibraltar Government and have turned it in to a very unique location which, of all our locations, has garnered the most applause and mythology. But of course this, often exaggerated, speculation has become a very important marketing tool and has served to showcase our technical abilities across the globe, and not just for eGaming companies.”

## The Isle of Man

Mr Tobin explained that the Isle of Man’s past economic development theme, ‘freedom to flourish’, was something that initially attracted Continent 8 to establish its headquarters in the well-respected jurisdiction. “In our technology based industry with an eGaming focus, our concern was ‘how do you take something as unregulated and seemingly unregulatable as the internet and combine it with

something that was almost overregulated, as land-based gambling then was?’. That’s the value proposition we had in the early days. This was born very much out of our experience in selecting a jurisdiction which allowed us to provide technical and regulatory solutions to our customers and the Isle of Man has since become a critical component in our network.”

## Malta

“Our decision to create a base in Malta was again in answer to the needs of our customers who were looking to establish themselves using an EU licence”, Mr Tobin explained. “We continue to operate in Malta and provide what is probably the best network for our customers there. The ease with which people are able to get on and off the island is also a major factor in its success, as it has been here in Gibraltar. Working closely with Gibtelecom, the fibre infrastructure we connected in to provided alternative routes even to our providers as well as managed networks.”

## Dublin

Mr Tobin explained that key factors in the decision to develop a site in Dublin this year include its technological renown as well as the importance of diversifying a company’s reach. “More and more people are in multiple locations, you cannot be reliant upon one single site”, he remarked. “So we provide that neutral vehicle for customers both in terms of their tactical and their regulatory needs and this extends to London, Paris, Guernsey and Montreal.”

## Points of Presence

“Points of presence where our network connects also serve as advanced locations where we can offer unique services to customers that need to be located in these jurisdictions. We are also in Belgium and Taiwan and, for the last couple of years, have also been dealing with a lot of data centre requirements for Las Vegas, Chicago and Miami in anticipation of inter-state lotteries, for example. A unique location that we’re just initiating at the moment is also the US Virgin Islands which can be, from our perspective, considered the US’s Malta. We’re working very closely with the US Virgin Islands Government to develop a product for them. In this case the government may want to outsource a lot of their IT management to us and this is, again, becoming a key business area alongside data management and protection. So in all cases, what we do is driven by our customers.”

## Client Services

“As many of you know”, Mr Tobin explained in closing, “client services overall are something that your market teams work very hard to identify and define. So we work very closely with our customers to provide case specific virtualisation solutions in multiple locations. In the sense that I mentioned earlier, we function very much as an entrepreneurial company. Operating online means you must be ready to react which is why we remain in close contact with jurisdictions and operators to respond to their needs. It is important to be an entrepreneur as the world changes and we continue to encourage the customer to make those associations with Continent 8.”

# The 4th Money Laundering Directive and Its Potential Impact to Online Operators

## Peter Howitt

Ramparts Law

“It is not clear why, in a directive which is basically saying ‘you do the work to find out what the risk is’, they see fit to hard-code measures which make it seem that gambling is a much higher risk than any other activity.”

Ramparts Law is a European law firm based in Gibraltar and specialising in cross-border corporate, commercial and regulatory matters relating to e-commerce, technology, gaming, financial services and tax. It was founded by Peter Howitt, a solicitor who has worked in the e-commerce, gaming and financial services sectors for over 10 years. The firm advises entrepreneurs and multi-national corporations (inc. NASDAQ and FTSE listed companies) in relation to local and international commercial projects. Peter qualified in England and Wales as a Solicitor in 2002 and in Gibraltar, 2012. Peter is also the Chief Executive Officer of the Gibraltar Betting & Gaming Association and the Secretary of the Gibraltar E-Money Association.

Mr Howitt opened his presentation with a brief explanation of the 4th Money Laundering Directive which, although still in draft form, is set to have a significant impact upon the online gaming and the financial services sectors. Mr Howitt observed that at a very high level the 4th Money Laundering Directive could be summarised as follows: “There is risk based evidence driven AML party in Europe... and nearly everyone is invited.”

### The Details

The 4th Money Laundering Directive, Mr Howitt explained, covers gambling entities and takes a very risk based approach (RBA), requiring lots of risk based assessments. Essentially an extension of the 3rd Money Laundering Directive (published in the Official Journal of the European Union on the 25 November 2005), it contains a number of practical elements that

have yet to be decided. In practical terms, it is unlikely to have an operational impact for obliged entities until after 2016. It is likely to impact regulators, governments, operators and licensed firms, and represents a significant gear-change to a more EU federal and state approach to AML, where all key stakeholders have obligations to a risk based approach. Overall, it is positive for the online gambling industry, Mr Howitt assured the Summit. This is due to the specific inclusion of online gambling in the directive for the first time, which enables the industry to demonstrate to those that remain sceptical of its integrity that it adheres to the same high standards as leading financial institutions. Mr Howitt emphasised, however, that it is important not to underestimate the potential risk of further cross-border legal confusion, the law of unintended consequences and the possibility of misuse of AML laws to restrain cross-border trade.

### Stated Objectives

The stated objectives of the draft are to:

- reduce cross-border complexity
- safeguard against criminality and terrorism
- safeguard economic prosperity
- contribute to financial stability and soundness of the financial system
- ensure consistency between EU and international rules (particularly the FATF recommendations)
- increase the consistency of national rules (although we’re still not seeing harmonisation, an evidence driven approach may facilitate a move towards this goal)





Peter Howitt

- introduce a harmonised criminal offence of money laundering across Europe (and certainty of the predicate offence of tax related crimes)

Whereas previously only land based casinos were covered in money laundering directives, all online gambling operators will be covered as part of the 4th instalment. The general approach of the directive, Mr Howitt explained, is to set some common standards but leave Member States, regulatory bodies and obliged entities, which include gambling operators, to take detailed risk assessments and ensure adequate measures are put in place which are commensurate with risk for country sectors, transactions and customers. "It is less prescriptive than the 3rd Money Laundering Directive in many ways and this is to be welcomed", Mr Howitt remarked. "It doesn't seek to set in stone a judgement on what is considered to be high or low risk but allows for a detailed risk assessment to be conducted at various operator, national and supranational levels. Most positively, it aims very much at cross-border implementation, sharing and standards, however with minimum legal harmonisation in most respects it could lead to greater inconsistencies."

## Main Changes

Mr Howitt explained that the use of simplified due diligence is to be significantly reduced. There is also a change in customer due diligence thresholds for cash transactions from €15,000 to €7,500 and a minimum set of principle-based rules for administrative sanctions. Tax crimes are now included as a predicate

offence for defining criminal activity and all companies are also now required to hold and share information on beneficial ownership. This is largely to ensure that there are no jurisdictions in Europe that can be compared to, for example, the British Virgin Islands.

National Risk Assessments are required and national measures are to be taken with closer cross-border co-operation between financial intelligence units, the European Banking Authority and other supranational bodies. "Quite frankly", Mr Howitt remarked, "cross-border issues between financial intelligence units have been a major problem in terms of reporting and the sharing of information and there has also, in the past, been a problem with knowing exactly who to report to."

Customer due diligence measures continue to allow for simplified, standardised and enhanced due diligence and it will also be much more evidence and multi-variant risk based when determining risk and the measures to be taken in mitigation. The use of the 3rd Country Equivalence White List has also been removed. This is due to the move towards a risk based approach. "Interestingly they have also removed the 'in principle' simplified due diligence waiver", he added.

There is to be an increase in PEP (Politically Exposed Person) checking, both domestic and international, which will lead to increased requirements for obliged parties to ascertain risk and mitigate against it.

## Gold Plating

Because it is not a maximum harmonisation directive, Member States can also gold plate the directive or implement it with additional measures. "This is something about which the industry should be very concerned", Mr Howitt urged the Summit. "This is not something that has been put there for the gaming industry, but is the result of public policy issues, however the ability to gold plate the directive upon transposition is obviously something that is open to abuse."

Member states are supported by supranational EU supervisory bodies, including the European Banking Association and Europol, and are also obliged to share assessments between each other. "This increase in reliance upon supranational bodies is one of the things I like most about the directive", Mr Howitt noted. "It is doing much more of the work in terms of harmonisation and coordination across borders than has been done previously. This will make it easier for industry operators within the sector to be able to gain a better sense of the otherwise fragmented AML environment."

## Recitals of Interest

Gambling is defined as 'any service involving wagering in games of chance including those with an element of skill such as lotteries, casino, poker and betting transactions'.

Mr Howitt noted that Recital 13 of the directive was interesting in its specificity, due to its stating that 'the use of the gambling sector to launder

“The major issues I see are that it is all about cross-border communication and compliance for the online industry. Some operators will already be more sophisticated than others and will be aware that they are already subject to AML in multiple territories.”

the proceeds of criminal activity is of concern’. “It is interesting in a directive that is predominantly evidence and risk based that we have this sentence, which gives no indication that it was based on assessment or evidence”, he remarked. “It is of some concern because it is a presumption.”

“Gambling operators are also going to be subject to a lower threshold for cash transactions. The normal threshold is €15,000, soon to be €7,500 but the gambling threshold is €2,000, which will be applied to wagers and winnings. It is not clear why, in a directive which is basically saying ‘you do the work to find out what the risk is’, they see fit to hard-code measures which make it seem that gambling is a much higher risk than any other activity.”

Recital 23 allows for obliged entities to rely on 3rd party introducers or partners to carry out customer due diligence, although regulatory obligations remain with the obliged party. Recital 31 provides for data protection for sensitive sharing of information for fraud prevention, although the current draft does not extend these measures to gambling obliged entities, only the financial institutions. Operators may still benefit from the inclusion of PSPs, “The industry must come together on deciding how to lobby for influence on this over the next couple of years, because there is no reason why gambling operators are included in many of the restrictive measures and then dropped for many of the benefits and rights contained within the directive”, Mr Howitt urged the Summit.

## Articles of Interest

Article 4 provides that Member States can extend the scope to more categories of obliged undertaking (gold plating) while Article 5 provides that Member States can also adopt stricter provisions. Article 7 states that Member State risk based approaches will be used to consider the application of these additional measures by local obliged entities. Member States must also ensure that obliged entities assess AML and terrorism financing risks, taking into account various factors including customers, countries, products, services, transactions and delivery channels, according to Article 8. “Interestingly, in Article 8, it may be appropriate to require an independent audit of these policies and procedures, the results of which are to be made available at all times. Operators should be aware of this change”, Mr Howitt advised the Summit.

## Germany

Moving towards a conclusion, Mr Howitt explained that “the major issues I see are that it is all about cross-border communication and compliance for the online industry. Some operators will already be more sophisticated than others and will be aware that they are already subject to AML in multiple territories. For others, it may come as a surprise that there isn’t as much harmonisation within European law as you would expect.”

“Under AML principles, the presumption is that the Home State regulator regulates obliged entities and the AML laws of that State. You should be aware that other states that you provide services to on a remote basis,

“Many countries did not support / understand the industry or approve operators for the sector and unfortunately the legislation was poorly drafted and had many unnecessary commercial restrictions.”

may implement a different approach. So, in addition to business and consumer laws, you need to be looking at the anti-money laundering requirements that are applicable in other territories. The use of Host State AML can also apply when you are using local agents - again depending on the approach by local Member States.”

## Electronic Money – lessons learned

“I don’t want to be considered scaremongering here when I talk about the risks to be considered,” Mr Howitt emphasised. “But, just briefly, in 2000 the 1st E-Money Directive came into force and intended to open up certain stored value payment products wider than just the banking sector. There was very poor uptake in Europe compared to that anticipated, with some notable exceptions such as in the UK private sector and the Italian public sector. Many countries did not support/understand the industry or approve operators for the sector and unfortunately the legislation was poorly drafted and had many unnecessary commercial restrictions. This forced the European Parliament to introduce the 2nd E-Money Directive in 2009 with maximum harmonisation measures to avoid fragmentation or the gold plating of some operational requirements.”

“Interestingly,” he continued, “despite the purpose of the 2nd directive clearly being to open up the market for regulated electronic money, in Germany they decided to use this as an opportunity to increase restrictions on electronic money. This was a shock: such a regulatory approach may be the norm for online gambling but it was not expected in the more integrated financial services sector. The e-money sector was already on its second directive with harmonisation measures intended to encourage that industry. Germany’s AML structure is based on the normal AML territoriality principle, which means they could not enforce the new AML provisions against foreign EMIs. Given Germany’s resistance to the e-money sector, however, it had no domestic EMI’s and many German companies had obtained a licence in the UK in order to passport back into their cultural home-base. Germany therefore focused on severe limitations for any locally established distributors or agents of EMI’s and made it almost impossible for EMI’s to work with local petrol stations, shops etc. where prepaid cards would usually be sold. The e-money sector tried to reason with the German authorities and it could be argued with some justification that Germany’s transposition looked like an exercise in bad faith given the purpose of the 2nd Directive. Germany was able to implement the 2nd Directive in such a way that it led to an estimated

decline of about 60% in the German e-money market. Ironically, therefore, Germany failed to support the e-money industry when it started, failed to grant e-money licences to local companies, failed to transpose European law requirements properly and then appeared aggrieved that it did not have control and oversight over its own domestic market who were transacting with EMI’s in other countries – a familiar story for online gambling.”

“With this in mind, the eGaming industry must, therefore, demand a supranational authority that is responsible for gambling in Europe. It must engage with relevant supranational bodies for gambling to issue guidelines on applicable AML rules for cross-border operators and to ensure no unwarranted extension of AML obligations to partners. Finally, it must prepare for the potential misuse and lack of understanding of the sector as well as the plain poor transposition of the directive in a manner that restricts cross-border operators, particularly where local gambling law restrictions are currently deemed unlawful under European law.”

# Unintended Consequences: The Pitfalls of Gross Profits Taxation and Similar Economic Strategies

## Sue Rossiter

Director of Projects and Policy  
Remote Gambling Association

## Simon Trussler

Director, Economics and Regulation  
KPMG

Sue joined the Remote Gambling Association in January 2012 where she is responsible for policy development, government relations and special projects. Previously she was Head of Policy at the UK Gambling Commission and headed up the Gordon Moody Association, which supports problem gamblers to overcome their addiction.

Simon is a Director in KPMG's Economics & Regulation practice. He is experienced at advising companies and policy makers on the economics of excise taxation in the gambling, alcoholic drinks and tobacco markets. He has also advised companies and tax authorities in numerous tax disputes including VAT, landfill taxation and transfer pricing cases. Simon worked recently for the Remote Gambling Association where he led a team analysing the economic impact on sports betting in Italy of a gross profits tax relative to a turnover tax. The report, which contained new and detailed economic research on the relative merits of the two taxes, built on earlier KPMG reports on the markets in Spain and Cyprus. Simon has also advised lottery operators on regulatory and commercial matters.

Sue Rossiter introduced the joint presentation as an examination of how the UK's proposed taxation regime and its tax rate levy may result in a range of pitfalls that undermine the UK Government's policy intentions. She explained that KPMG has undertaken a number of studies for the Remote Gambling Association (RGA) on the taxation of remote gambling in various jurisdictions and drew the attention of the Summit to a recent report entitled 'An assessment of the impacts of a gross profits tax on Italian sports betting'. Ms Rossiter explained that the report was issued to a Spanish regulator to submit that new tax levels are required to prevent the rise of unlicensed operators and had been very well received in both technical and local press.

Ms Rossiter then identified four key factors which inform an individual's decision to bet with a given operator; three of which are influenced by tax:

- the quality of the online experience: including ease of use, availability and social experience
- prices: including pay-out ratios, cost of sign-up, rates
- advertising and marketing: brand recognition
- bonuses, free bets and top-ups: used to attract, retain and revive customer accounts

## Additional Taxation

"For the most part," Ms Rossiter observed, "it is the discretionary spend that is influenced by a raise in tax levels on a particular product, so there is little change to the quality of the online experience. The development of a site is usually a sunk cost and is not very frequently impacted by additional or ongoing expense. It's the three other areas that do have an impact on the customer: prices will rise as the tax is passed on to them, advertising will be reduced, and top-ups and bonuses will also be reduced as discretionary spend falls."

Mr Trussler then took over from Ms Rossiter in explaining some of the conclusions of the economic and market data research conducted in partnership with the RGA over the past few years. "The results and findings we're going to be talking about are very, very robust and take into account detailed economic theory, socio-economic research, economic and market data, and are scalable to changes in the market structure - whether it's a monopolistic market or a competitive market, or somewhere in between," he assured the Summit.



Sue Rossiter



Simon Trussler

“But before I go into conclusions it’s worth thinking about the different types of tax that are contenders”, Mr Trussler emphasised. “The first type of tax is the turnover tax, which is a tax on stakes or gross money wagered before payout [tax revenues = tax rate x stakes]. The second type of tax is the gross gaming revenue tax, which is a tax on stakes less prizes or gross money wagered after payout but before expenses [tax revenues = tax rate x stakes x (1-PPR)]. The reason I bring this tax up is that gross gaming revenue taxes are often talked about as if they are a gross profits tax, but a gross gaming revenue tax is different because it’s a tax on stakes less prizes. Finally, a gross profits tax is a tax on gross gaming revenue less other operating costs, and those operating costs involve the cost of serving a customer or providing a transaction, and may also include, for example, some proportion of IT costs and service costs as well as the important other costs like bonuses and free bets. These are all important costs for gambling operators.”

Mr Trussler then explained that the first fundamental about the turnover tax is the formal incidence on the gambling operator. “Effectively”, he remarked, “for every Euro staked the operator

has to hand over a certain number of cents depending on the tax rate. So in that respect it’s no different from an increase in the marginal costs of operating a business. Now, a profit maximising company balances two things when faced with an increase in cost. First, the gaming operator will try to pass on that cost to the customers to preserve its margin, but the consequence of that is lost sales. Second, maintaining sales and market share. So what one would normally expect to see in the case of turnover tax is some pass-on, but not necessarily full pass-on, and the extent to which this pass-on will take place depends on the nature of the market and the price sensitivity of customers.”

The similarity between the turnover tax and the gross profits tax is that the formal incidence again lies with the gambling operator, Mr Trussler observed, “but that is pretty much where the similarity ends. The gross profits tax is a tax on the gross profits of the industry, and if there are no gross profits attached to an extra sale there are no taxes imposed. There is no way that a gambling operator could increase its prices after the imposition of a gross profits tax and increase its

profits. Under a gross profits tax regime, we would expect the same prices to the customer and the same sales figures as without the tax.”

## Initial Propositions

“So our first conclusion is that the turnover tax is expected to result in higher prices and lower sales volumes and the gross profits tax does not. Our second conclusion is that the gross profits tax is capable of raising more tax revenues from individual firms than the turnover tax. This is because lower sales result in a lower tax base.”

“Our third proposition is that there will be at least as many active firms under a gross profits tax as under a turnover tax regime”, Mr Trussler continued. “The logic behind that is under a gross profits regime there will be a higher price/payout ratio, so a higher total market demand. It must, therefore, be possible for at least as many firms to operate under a gross profits tax.” Mr Trussler then observed that it follows from propositions two and three that more tax revenues can be raised from a gross profits tax than from a turnover tax and reiterated that

**KPMG**

*cutting through complexity*



“what we need to see are ways of ensuring that consumers who turn to the internet to gamble are afforded the protection they need while governments get the duties they are owed.”

this conclusion is backed up from detailed economic theory and market analysis. “This is not to say that there will be no distortions to the market under the gross profits tax but that we would expect the largest market distortions to come from the turnover tax, and the lowest potential tax revenues as a consequence.”

“The fifth and final proposition is that the greater the threat of gamblers switching to offshore, duty-avoiding alternatives, the more turnover tax revenues will be eroded”, Mr Trussler explained. “And this, as DLA Piper noted this morning, is because you can’t fight gravity. If people can swap to a cheaper, duty avoiding alternative they will do it. If any organisations have a chance to turn a profit by serving that need, they will do it. For hundreds of years, with tobacco and alcohol, this has been the case. From a policy point of view that means that as more gamblers switch offshore, the tax base will be reduced and frustrate the Government’s revenue raising policy objectives. It also means that some gambling activity potentially goes unregulated – so there is everything to lose when you get the tax rate and structure wrong.”

## Internet Penetration and Tax Structures

Taking over from Mr Trussler, Ms Rossiter explained that online gambling was not born out of the desire to avoid tax but was the result of the efficiency with which individuals could gain access to a popular market product. Rising levels of internet penetration in both the developed and developing world, she observed, also mean that as individuals gain increased access to the internet so too is there an increase in providers of online services.

Turning the attention of the Summit to a recent KPMG report entitled *Online Gaming: A Gamble or a Sure Bet?*, Ms Rossiter then explained that there was, until recently, limited opportunity for gamblers to switch to offshore duty avoiding alternatives. “One of the key findings”, she continued, “was that the gambling industry is progressively moving into new markets, those markets are increasingly being licensed, and what we need to see are ways of ensuring that consumers who turn to the internet to gamble are afforded the protection they need while governments get the duties they are owed.”

“Internet penetration is growing in line with the increased availability of technologies and services as well as global population figures”, Ms Rossiter continued. “So what we’re seeing here is more people coming online, more people gambling online, and the potential for more revenue to be collected. We expect numbers to increase and we expect more people to come from unregulated jurisdictions to fill in the gaps where there aren’t efficient controls.”

## The Laffer Curve

Mr Trussler then took over in explaining that it is not important simply to implement the right tax structure, it is also important to ensure that the tax rate is properly set. Under any form of tax, he observed, an excessive tax rate has the potential to distort the market, have unintended consequences and frustrate policy objectives. “The most famous articulation of the relationship between tax rates and tax revenues is known as the Laffer Curve. It is famous not because Arthur Laffer invented it, but because Laffer drew the curve on a napkin in the 1970s, showed it to Donald Rumsfeld, and it informed a large part of United States fiscal policy throughout the 1980s.”

The vertical axis of the Laffer Curve graph showed tax revenues and the horizontal axis showed the tax rate. A zero tax rate therefore shows zero tax revenues because there is no tax base. Equally, if tax rates are too high, there will also be no tax revenue because consumers will not make any purchases, either because they simply stop buying or switch to an alternative product.

“When you start from a zero tax rate and you increase the rate a little bit, it will increase the price of the product or service by a little bit, so tax revenues will go up a little bit”, Mr Trussler explained. “If you increase the tax again, it will increase a little bit again. Some people will stop buying the product or service because of an increase in price, but not very many. But if you carry on increasing the tax rate, it will erode sales by so much that successive tax rates will eventually start to decrease revenues. Between these two extremes there is a curve - the Laffer Curve - and there is a sweet spot at the apex which is the tax revenue maximising rate of taxation.”

“One of the things that concerns us, if they are included in the taxable base, is the bonus. It’s what customers expect, it’s part of an operator’s retention strategy and we believe that an operator’s marketing strategy should be considered exempt from tax.”

“The application of the Laffer curve to a turnover tax on online gambling is obvious. The Laffer curve tells us that it is important to not set an excessive tax rate. This applies equally to a gross profits tax, but the mechanism is a bit different. We all know that operators invest in customers by advertising and promotions and the payoff is profits from new customers. There are also further investments in bonuses and other promotions to maintain and grow customer demand, so we make an investment for future payoff. Anything that reduces that payoff reduces the incentive to invest in new customers and maintain or grow the business and this will reduce the tax base as a consequence. An excessive gross profits tax will erode operators’ incentive to acquire and maintain customers by such a large amount that total tax revenues will be undermined. So, again, there is a tax rate that balances higher tax revenues per unit of sales with maintaining a sufficiently large tax base.”

Mr Trussler then remarked that the increased availability of offshore (unregulated) operators exacerbates the problem. Increased availability of a lower priced supply pushes the sweet spot down and to the left towards lower rate and lower revenue levels: “so if you get the tax rate wrong now, with an increasing availability of duty avoiding offshore gambling operators, it’s almost inevitable that the problem of customers switching to lower priced, duty avoiding alternatives will grow. And that’s why I think tax authorities need to take this quite seriously.”

## In Closing


Moving towards a conclusion, Ms Rossiter explained that tax is not the only thing that affects the costs of a business. The full range of costs to a regulated operator include licence fees, gambling taxes, administrative costs, compliance costs, business taxes, amongst others, meaning that tax needs to be considered holistically and be administratively efficient.

“One of the things that concerns us, if they are included in the taxable base, is the bonus,” she explained. “It’s what customers expect, it’s part of an operator’s retention strategy and we believe that an operator’s marketing strategy should be considered exempt from tax. Another issue surrounds consumer protection. For most governments the regulation of online gambling is not just about taxation and a licensing regime allows consumer standards responsibility. If consumers are forced to gamble offshore, however, then those benefits that the Government hopes to introduce will not be shared.”

“Administrative efficiency is also important,” Ms Rossiter continued. “It’s no good having a relatively low level of tax if the cost of collecting it is very high, so we say keep it simple, ensure low costs of collection are passed on, and encourage electronic registration and returns filing.”

“Finally,” Ms Rossiter added, “with the point of consumption tax comes the risk of double taxation, which is a major issue for multinational companies. Mutual recognition of double tax regimes is, therefore, very important and, where appropriate, there needs to be double taxation relief otherwise there may be casualties within the industry.”





“The application of the Laffer Curve to a turnover tax on online gambling is obvious. The Laffer Curve tells us that it is important to not set an excessive tax rate.”

# Afternoon Panel Session: The Outlook for Gaming

Moderated by:

Peter Montegriffo - Partner, Hassans

Peter Howitt - Secretary, GBGA

Kevin de Haan QC

Adam Craig - Group Director of Tax, bwin.party

Michael Carlton - Chief Executive, Victor Chandler International

**Peter qualified as a Barrister in 1982, becoming a partner of Hassans in 1988. His area of expertise is in commercial, gaming and private client matters. He has also been closely involved in drafting numerous changes to Gibraltar's legislation in trusts, financial services and gaming areas. Peter's knowledge of these fields has led him to contribute to a large number of articles and books on Gibraltar's legal system and financial services sector. He has also regularly spoken at international conferences relating to these areas of practice. Peter was Gibraltar's Minister for Trade and Industry, with responsibility for economic development and financial services between May 1996 and February 2000.**

Before inviting each of the panellists to identify, in swot analysis terms, the weaknesses and threats within today's eGaming industry, Mr Montegriffo observed that in an 'existential sense' the sector is one that not only continues to innovate and grow but is also here to stay. "The question, therefore, is what the sector will look like in five or ten years' time", he remarked. "In that respect, we will address the regulatory landscape, the issue of taxation, and the impact of technology in facilitating change and

the adaptation of the industry. Then there is, of course, the impact of social gaming which will undoubtedly have a transformational effect on the industry and its competitive environment."

## **What are your views on the threats or weaknesses we face in the eGaming industry?**

**Peter Howitt:** Mr Howitt opened by first addressing his concern about anti-money laundering legislation and its potential misuse. "Operators face the threat of simply not getting the requisite support at European level. The UK's bill demonstrates, for example, that territories which had previously been leaders in free market regulation will risk damaging their reputation and industry with questionable measures. Overall, I think we all know that the issues lie with a lack of understanding of online gaming at political level and, with respect to the potential for lobbying et cetera, a lack of commercial awareness of the issues at stake. I'm not sure that people within the European Parliament and the Commission always understand that, in their efforts to deal with sometimes quite parochial concerns, they are perhaps losing sight of other positives that European companies are leaders of, and that's something we need to think about in

terms of leadership, employment, taxes and all the things that go with them."

**Adam Craig:** "Fragmentation also brings with it a high level of complexity", Mr Craig added. "And, of course, taxation adds to that complexity and creates a new challenge to our operating model. It starts with Italy and France, and then Spain follows and the UK follows and you suddenly encounter a fundamental challenge to the economics. What that means is all those things that were core to our business model, such as affiliates and bonuses, have to go all because of the tax pressures imposed on margins."

**Michael Carlton:** Mr Carlton explained that, despite the regulatory and tax aspect being important factors to focus upon, it is also important to consider the impact of inconsistency in regulation across territories. "Regulation is something we all look for and respect", he observed. "It strengthens our products and our procedures, but when it becomes inconsistent and you're operating in multiple jurisdictions it becomes very difficult. That then leads to a deflection of resources from positive, commercial, money making activities to compliance and regulatory activities."



“Operators face the threat of simply not getting the requisite support at European level. The UK’s bill demonstrates, for example, that territories which had previously been leaders in free market regulation will risk damaging their reputation and industry with questionable measures.”

“Regulation is something we all look for and respect,” he observed. “It strengthens our products and our procedures, but when it becomes inconsistent and you’re operating in multiple jurisdictions it becomes very difficult.”

All of us spend a tremendous amount of time dealing with regulation and compliance in multiple jurisdictions and I’ve been sitting here thinking ‘why would anybody want to enter this industry now?’ We want to encourage good people to come into this industry but we’re putting up barriers to stop them.”

**Kevin de Haan:** “Good operators want to be regulated,” Mr de Haan began. “No-one wants to operate in the Wild West and I think that one of the greatest challenges the industry faces is in educating people to that end. I never cease to be shocked at some of the rubbish I read in the press and even sometimes in official documentation. I don’t recognise what’s being said about online gambling in the public sphere. So I think it’s not just a legal campaign, it’s a hearts and minds campaign to educate people that this is a compliant industry that is not out to seduce the vulnerable gambler or bring in the young gambler to the industry, quite the opposite in fact. So I think education is absolutely key.”

#### **What is the likelihood of the UK introducing a point of consumption tax regime?**

**Kevin de Haan:** Mr de Haan expressed his view that although it is theoretically possible, the introduction of a point of consumption tax is unlikely. “I say that because from a practical standpoint it is so much easier to impose a tax regime on an overseas operator if you require them to be licensed within the jurisdiction, because you automatically have a presence. The licensing system in the

UK automatically triggers an obligation to register with HMRC for general betting duty or gaming duty or whatever. So I think that it is an unlikely scenario but theoretically possible for those reasons. The practical obstacles to it are considerable.”

**Adam Craig:** “I don’t share the optimistic view of Kevin I’m afraid,” Mr Craig warned the Summit. “I think that HM Treasury would eagerly implement a tax knowing that it might only be able to collect from the bigger operators and deal with the consequences afterwards. There is currently no impediment, there are big numbers at stake and there is a feeling amongst some political figures that in some ways the coming situation is fair, even if they don’t really know how to make it legally fair.”

**Michael Carlton:** Mr Carlton agreed with Mr Craig, adding that there is a political will and desire to fix a remote angle, whether legally possible or not, and push the measure through.

**Peter Howitt:** Mr Howitt added that the UK measure was in line with the potential for countries to concentrate less upon the regulatory issues and more upon taxation.

**Kevin de Haan:** Mr de Haan agreed, stating that “there is perhaps one other political dimension to this in that the Government has pitched its flag to this particular vehicle of introducing a tax on the back of regulatory change. This whole basis for the imposition of new regulation is flawed but we have to remember that the hourglass for this particular administration is running

out. Who knows what we’ll see when we have a general election? I imagine the political landscape will be very different, we may even be talking UKIP and a flat tax,” he remarked.

**Adam Craig:** Mr Craig then took the opportunity to remind the Summit of a very important forthcoming VAT change which will provide that VAT be charged on a place of consumption basis. “In the past we may have been able to convince ourselves that we’re dealing with exempt supplies but it may well be that Member States begin to take a different view, if they haven’t done so already, on that particular issue as far as electronically supplied gambling is concerned. I also think it’s no coincidence that the point of consumption tax is supposed to be introduced at roughly the same time as this VAT measure will be coming in.”



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## Kevin de Haan QC

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“What’s going on here is a solution looking for a problem, and the problem isn’t there.”

**Can I ask about competitive threats in terms of the position in Europe: how do you see the competitive undermining of the European industry playing out and from where do you think the real threats are coming?**

**Adam Craig:** “I think that private operators may have more courage to pursue opportunities in markets that public companies no longer really focus on. The public operators are much more interested in focusing their resources on those jurisdictions which are taxed and regulated: the US market, for example.”

**Are we effectively throwing the towel in on a pan-European regime?**

**Michael Carlton:** Mr Carlton expressed his regrets that, in his opinion, regulatory fragmentation will remain throughout Europe; however he remained positive that there is a growing understanding about shared issues between licensing jurisdictions. “I think the current economic pressures that individual countries are facing are forcing them down a particular route at the moment”, he warned the Summit. “It’s very difficult to move from that when you have economic demands placed upon you that force you to act in a certain way. I think there is a general understanding but I don’t think anything will happen over the next five years.”

**What significance do you attach to the UK’s role in this?**

**Michael Carlton:** “I think it’s disappointing for a country that has been at the forefront of regulation, in the same way that Gibraltar has for the last 20 years or longer, to suddenly turn its back on that successful model. It’s a shame and a lost opportunity.”

**Kevin de Haan:** “And it’s for no good reason, that’s the point here”, Mr de Haan agreed. “The UK has had the freest, most open and most diverse gambling market in Europe for decades and we’ve had the lowest incidence of problem gambling, of penetration by criminal elements, and so on. What’s going on here is a solution looking for a problem, and the problem isn’t there.”

**Where do you see the new opportunities in today’s marketplace?**

**Adam Craig:** “Operators will have relatively unknown new competitors in the US such as Caesar’s and MGM and so on”, Mr Craig remarked. “Especially for the public operators, the US is going to be very capital intensive and demand a high degree of focus on our own businesses. We are in a very secure position with the licences we have in our core jurisdictions, but we are faced with a lot of distractions that take away the excitement of some of the emerging markets such as China that some privately owned companies enjoy and which we can’t touch.”

**Michael Carlton:** Mr Carlton agreed with Mr Craig in that there are various opportunities to make emerging markets more easily accessible to the incumbent operator. “I think we have to look towards consumer behaviour and how that’s changed with the introduction of mobile, for example, which is the latest major opportunity. I’m amazed at the industry and how adaptable and innovative it really is, and I think that as long as we retain that creativity we can respond to new opportunities. That’s where the growth will be and we have to take advantage of that.”

**Kevin de Haan:** “China is a vast untapped market with huge potential and if that ever opens up it will change the landscape beyond recognition”, Mr de Haan added.

**Adam Craig:** Mr Craig agreed with the imperative to respond to cultural changes in the marketplace, remarking that “our sector is still pushing poker and slot machines; it’s no wonder we’ve been taken by surprise by social gaming. With social, gaming is exciting again and it’s accessible.”

“China is a vast untapped market with huge potential and if that ever opens up it will change the landscape beyond recognition.”

**How potent is social gaming to operators as they diversify into broader forms of entertainment?**

**Michael Carlton:** “I think it’s one of the tools we have to look at,” Mr Carlton urged the Summit. “It’s now a natural extension of the ways in which people communicate with one another, just as they do using a telephone or face to face. You can’t ignore it, you have to embrace it, and the key, although I’m not quite sure what that key looks like at the moment, is how you monetise it.”

**Peter Howitt:** Tackling the topic from a legal perspective, Mr Howitt approached social gaming in light of the approach to categorisation of gambling as a form of financial service. “With financial services you have a tiered approach to a range of activities, it’s not all or nothing, and for those who have gone to the expense of having a gaming licence I think being able to provide the backbone for social gaming operators would be beneficial to help manage the regulatory issues concerning social gaming.”

**Kevin de Haan:** “We may have a sleeping crocodile syndrome here where suddenly someone will wake up and snap and we’ll suddenly be stuck with a load of new proposals,” Mr de Haan agreed. “I think this lack of understanding will pose a problem to gambling regulators and we need to watch this space, particularly as social gaming is something that is attractive to a younger audience than perhaps we’re used to in conventional online gambling. I also think that the way in which the industry handles social gaming is going to be key to the reaction of the regulators. There is no doubt that there is a huge window of opportunity here.”

**Question from the floor: What is the likelihood of Europe really engaging with regulators in forming something which resembles a pan-European regulatory regime?**

**Kevin de Haan:** Mr de Haan remarked that, in his opinion, the formation of a cohesive pan-European regime is a real possibility, however one that is not going to happen for the next five to ten years. “I think, ultimately, it’s a solution that has to be adopted because this fragmentation cannot go on indefinitely, particularly as the European Union expands.”

**What significance do you attach, if any, to the possibility of infringement proceedings against Member States being relaunched by the European Commission?**

**Kevin de Haan:** “I would say they need to get on with it. They may have been announced in October but some of these proceedings have been running for some considerable time. I know that it takes a long time for these things to happen at Commission level but we’re coming now to three or four months after the announcement and I don’t see any movement. If they’re serious about it, they need to do it.”

**Are there any other obvious technological leaps that the industry is adopting other than mobile?**

**Peter Howitt:** “The obvious one to me seems to be the increased use of the Cloud and what it has brought to the industry. It is enhancing our ability to control cost and scalability as well as slice and dice data to put it in various locations depending upon regulatory requirements. It can be hugely cost effective and can have significant tax advantages depending on where you

put your data packets. There are lots of things that you can do with cloud technology which can have significant benefits to the industry.”

**Adam Craig:** Mr Craig added that there are also some quite high barriers to entry in the market and that internet sourced or crowd funding opportunities are a particularly new and exciting complement to the eGaming industry.

**With reference to the 4th Money Laundering Directive: how important is it that gambling has been brought into the mainstream through inclusion in such regulatory measures?**

**Peter Howitt:** “I hope I haven’t come across as being too negative because overall I do think it’s a good thing for the industry,” Mr Howitt enthused. “There are some risks as we’ve seen with the German e-money example and I think operators need to be aware of this. That is why it is important to develop relationships between stakeholders to make sure that we do have these supranational bodies who can be responsible for lobbying and for saying ‘this really is nonsensical’ or ‘this could help the industry if approached in this particular manner’. It is true that a large part of the approach to the industry has thus far not been based on any evidence and we need to be in a position to educate and guide people towards that end. Due to the evidence based approach that will be required, bringing eGaming into the AML fold can only be a good thing for the future of the industry.”

# Closing Words

## Russell Kelly

Director: Audit & Advisory

KPMG Isle of Man

**Russell joined KPMG in 1993 and has worked for KPMG in the Isle of Man, Gibraltar, London and Jersey. His client experience encompasses financial services, telecommunications, real estate and e-gaming.**

**Russell also undertakes transaction services and ISAE3402 work which includes acting for clients with respect to acquisitions, disposals and flotations; in particular he has advised on flotations on the LSE, AIM, Luxembourg and New York Stock Exchanges. Russell acts for a number of e-gaming operators and key service providers to the e-gaming sector in the Isle of Man and Gibraltar.**

Mr Kelly concluded the day's events by drawing a parallel between discussions surrounding the likelihood of pan-European regulatory cohesion and his own experiences within the financial services industry over past decades. "I think I concur with you in that I wouldn't hold my breath on the prospect of pan-European harmonisation. If we look at the financial services industry, despite the European Commission's categorisation, we're still trying to harmonise that industry 30 years on so, as Kevin said, we could well be facing a ten year wait before any meaningful developments take place."

Mr Kelly continued in observing that this year's event marked the third in a series of KPMG eGaming summits in Gibraltar, which have swiftly become some of the most popular and engaging events in the industry calendar. "The industry is so fast paced and so kind to us, really, with its different innovations and challenges that putting a programme together is relatively straightforward," he remarked, "there is always something of great interest to talk about and I am confident that we will be able to field an equally fascinating and expert selection of speakers on topics equally pertinent to the industry, both globally and domestically, this time next year."

Mr Kelly then took the opportunity to thank the day's sponsors - Hassans, Callcredit, Counting House, Continent 8 Technologies, Intelligent ID and Gibtelecom - for their generosity and support throughout the process before expressing his gratitude to the speakers and panellists who helped make this year's eGaming summit yet another resounding success. "Finally I would like to say a big thank you to my team at KPMG and at Ashgrove Marketing for putting all of this together," he added.

In closing, Mr Kelly took a moment to reiterate KPMG's commitment to Gibraltar and to explain the team's position on what he described as "a jurisdiction which remains at the forefront of the eGaming industry both in terms of the quality of its technological infrastructure and e-business community, and the lasting integrity of its regulatory regime."

"A lot of you may know that we re-established our offices here in 2008 and Micky Swindale has been instrumental to our position here over a number of years," he enthused. "I am pleased to announce that Micky has been appointed as Managing Director of our Gibraltar practice and will be working with the support of our resident team both here and in the Isle of Man. I would like to offer my congratulations to Micky and my thanks to all of you who here today. We look forward to seeing you all next year."



## Russell Kelly

Director: Audit & Advisory  
KPMG Isle of Man

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