



## The Antigua-United States Online Gambling Dispute

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### ***Abstract***

During the last decade, online gambling grew in popularity while complex and overlapping gambling laws in the United States left its legal status ambiguous. The United States' efforts to prosecute foreign-based suppliers of online gambling services prompted Antigua to file a complaint in the WTO, in which it claimed that the United States had violated its GATS commitment to free trade in recreational services. The WTO ultimately ruled in favor of Antigua and awarded Antigua the right to suspend \$21 million annually in intellectual property rights held by U.S. firms. This dispute exemplifies the potential for market access commitments to have unexpected and undesirable consequences. The potential for suspending intellectual property rights as a retaliatory measure may increase the leverage of small countries in trade disputes with large countries, but the implementation and management of such a suspension may be difficult and costly.

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## Overview

The online gambling dispute between Antigua and the United States illustrates key issues in international trade, including the relationship between domestic legislation and international agreements, the potential for trade commitments to have unintended consequences, and the challenges facing small countries in disputes with large countries. And it has culminated in an intriguing and unintuitive decision: the World Trade Organization empowered Antigua to suspend intellectual property rights held by U.S. firms. In this article I survey the relevant background, outline the sequence of events in the online gambling dispute, and discuss some of the issues raised by this case.

## Background

Antigua and Barbuda are tropical Caribbean islands covering 443 square miles (about 2.5 times the size of Washington, D.C.) (CIA 2008). The two islands are organized as a single political entity, hereafter “Antigua.” Antigua’s 2007 population was 69,500 persons, and its gross domestic product (GDP) adjusted for purchasing power parity (PPP) was \$1.2 billion, giving it a high GDP per capita by Caribbean standards (CIA 2008). More than half of its GDP is generated by tourism, with one third of its tourists coming from the United States (CIA 2008).

Since the late 1990s, companies based in Antigua have used Antigua’s high-quality international fiber-optic cable connections to provide gambling services over the Internet (Krebs 2003). The online gambling industry is the second-largest employer in Antigua after tourism; in 2001, there were 93 licensed gambling organizations in Antigua employing 1,900 persons (Antiguan Directorate of Gaming n.d.). Antigua’s annual online gambling revenue peaked at \$90 million in 1999 (Hansen 2006). There are conflicting estimates of how much of this revenue came from gamblers in the United States, but Bear Stearns estimated that 60 percent of worldwide online gambling revenues came from U.S. customers in 2003.<sup>2</sup>

Online gambling is a relatively recent phenomenon (the first Internet casino was launched in 1995) facilitated by the expansion and improvement of communications technology.<sup>3</sup> Internet betting parlors offer a nearly

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<sup>2</sup> Cited in Kanigher, 2003.

<sup>3</sup> The Gaming Club, <http://www.thegamingclub.com>, was the first online casino.

unlimited volume of gambling services at very high speeds to customers around the world. Gamblers typically upload funds to the online gambling Web sites via electronic payment services or wire transfers, play games either with each other (poker, sports betting) or against the house (blackjack, roulette), and withdraw any winnings by check or online payment service. Online casinos have many competitive advantages over traditional brick-and-mortar casinos: U.S. resort casinos incur construction costs of up to \$300 million and generally operate with profit margins between 8 percent and 16 percent, while one representative online casino (Internet Casinos Inc.) was developed for \$1.5 million, employs 17 persons, and averages a 24 percent profit margin (Kyros n.d.).

U.S. policymakers have several concerns about online gambling. Some object to gambling in general, based on the need to protect the public from addictive behaviors that create negative externalities (such as bankruptcy) (Leach and Carruthers 2006). These objections are heightened with respect to online gambling, which is believed to be dangerously available to children, as users often can place bets with only a credit card number. Online gambling has become popular on college campuses, and the National Council on Problem Gambling estimates that 7 percent of college students who gamble online become addicted (Hogan 2007). There are also concerns specific to offshore online gambling, including the prospect of criminal organizations and terrorists using gambling Web sites to launder money (Leach and Carruthers 2006).<sup>4</sup>

Many countries, including the United States, have laws to control or prohibit online gambling (GAO 2002, 45). However, the borderlessness and anonymity of online gambling make it inherently difficult to regulate. For example, Internet gambling sites can prevent banks from recognizing transactions as gambling by disguising credit card transactions or using online payment providers as intermediaries (GAO 2002, 21). Most online gambling companies are based in small countries (Antigua, Costa Rica, Malta, the Isle of Man, etc.) with limited ability or inclination to supervise the industry.

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<sup>4</sup> However, gambling websites keep detailed records of every bet and some have expressed willingness to share their records with U.S. regulators; see Kanigher.

## Ambiguity in U.S. Gambling Laws

The complexity of U.S. gambling laws adds to the difficulty of managing online gambling. For one, there are overlapping federal and state regulations. States determine whether individuals are permitted to gamble, and whether gambling businesses are permitted to operate, within their borders (GAO 2002, 3). (As of 2006, 8 states—Illinois, Indiana, Louisiana, Nevada, New Jersey, Oregon, South Dakota, and Wisconsin—had specifically prohibited internet gambling (Friedman and Cheng 2006).) On the other hand, federal authorities are responsible for regulating interstate commerce, which is often interpreted to include online gambling (GAO 2002, 12). As an example of the tension between state and federal authorities, in 2001 Nevada Governor Kenny Guinn signed a bill establishing a legal framework for internet betting parlors, giving the Nevada Gaming Commission power to “adopt regulations governing the licensing and operation of interactive [online] gaming”(Richtel 2001). The Commission, however, has never used this power, because the Department of Justice (DOJ) takes the position that all online gambling is illegal, regardless of the laws of the state in which it takes place (Kanigher 2003).

The basis of the DOJ’s position is the 1961 Wire Act, the federal statute most directly relevant to online gambling.<sup>5</sup> This law prohibits the transmission of certain types of bets via wire-based communication networks (such as telephones). The view of the DOJ (as articulated in 2002 by then- Assistant U.S. Attorney General Michael Chertoff) is that the Wire Act “prohibits gambling over the Internet, including casino-style gambling” and covers jurisdictions both “where the bettor is located and the state or foreign country where the gambling business is located,” as opposed to applying only where bets are received (Kanigher 2003). However, the Wire Act predates the internet, and there are different interpretations of its application to online gambling. A 2002 federal ruling in Louisiana, later upheld by the 5<sup>th</sup> U.S. Circuit Court of Appeals, determined that the Wire Act only applies to bets placed on sporting events.<sup>6</sup> Additionally, some court decisions have affirmed that interstate gambling does not violate the Wire Act if gambling is legal both where the bet originates and where it is received.<sup>7</sup> This brings up the jurisdictional problem of defining location when electronic signals

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<sup>5</sup> Sporting Events – Transmission of Bets, Wagers, and Related Information Act, Pub. L. No. 87-216, § 2, 75 Stat. 491, 552-553 (1961).

<sup>6</sup> Thompson v. Mastercard International (2002), cited in Kanigher.

<sup>7</sup> United States v. Kaczowski (2000) and Missouri v. Coeur D’Alene Tribe (1999), cited in GAO.

are routed through telecommunications networks: an online bet could be made by a user in a gambling-friendly state, on the website of an internet betting parlor based in a gambling-friendly country, but comprise information routed through places where gambling is illegal.

The unresolved status of online horseracing wagers compounds these legal ambiguities. In 1978 Congress passed the Interstate Horseracing Act, 15 U.S.C. § 1978 (IHA), which allows the electronic transmission of interstate wagers on state-licensed horse races, so long as the relevant racing commissions and associations approve the transaction. Over the objections of the DOJ, Congress amended this Act in 2000 specifically to allow wagers placed over the internet (Rodefer 2005). The availability of online betting on horse races has helped the horseracing industry; in 2005, off-track and online betting on horse races generated \$3 billion in revenue, and online betting has been described as the source of “the only growth in the horseracing industry today” (Vlahos 2005). Despite this amendment, the DOJ testified in 2000 that it still believes internet bets on horseracing violate the Wire Act, pointing out that the IHA is a civil statute (allowing states, associations, and race tracks to bring civil actions against establishments that violate it) and thus does not override a criminal statute like the Wire Act (GAO 2002, 43). Nevertheless, the DOJ has never brought a case against a state-licensed entity offering online wagering on horse races. Representative Barney Frank, who sponsored a bill to legalize online gambling, recently said “you can't get a straight answer if [online betting on] horse racing is illegal. It's total hypocrisy and mishmash” (Gaul 2008b).

## **Chronology of the Dispute**

The United States started cracking down on foreign-based internet betting parlors in 1998, when federal prosecutors charged 21 U.S. citizens connected to offshore internet gambling with violations of the Wire Act (Hansen 2006). Among them was Jay Cohen, an American citizen and former stock trader who had been operating the Antigua-based World Sports Exchange (which had 10,000 customers that year) (Kanigher 2003). Twenty of the indicted persons entered guilty pleas, had their cases dropped, or remained outside the United States as fugitives, but Cohen returned to the United States to contest his case in court (Brunker 2001). He lost in 2000 and was sentenced to 21 months in prison and fined \$5,000, becoming the first person convicted in the United States for operating an offshore internet gambling website (Hansen 2006).

Cohen's case was brought to the attention of Mark Mendel, an attorney based in El Paso, Texas. After researching World Trade Organization (WTO) documents Mendel came to believe that the United States had violated the General Agreement on Trade in Services (GATS). He outlined his case in a memo sent to the government of Antigua, and Antigua's prime minister hired Mendel to file suit against the United States at the WTO (*Gaming Law Review* 2006).

In March 2003, Antigua initiated the dispute resolution process of the WTO to challenge the United States' prohibition on the cross-border supply of online gambling services. A Dispute Panel ("Panel"), formed in June 2003, determined that the United States had made a commitment to free trade in online gambling services in GATS Section 10.D, "Other Recreational Services, Excluding Sporting."<sup>8</sup> The Panel found that three U.S. federal laws, including the Wire Act, contravened this commitment (the other two were the Travel Act, 18 U.S.C. § 1952, and the Illegal Gambling Business Act (IGBA), 18 U.S.C. § 1955). State laws in Louisiana, Massachusetts, South Dakota, and Utah were also found to obstruct free trade in online gambling services. The Panel determined that the cumulative effect of these laws was inconsistent with the United States' commitments under GATS, and made a confidential ruling in favor of Antigua in March 2004. The Panel's report was released publicly in November 2004 after unsuccessful negotiations between the parties.

In January 2005, the United States appealed this ruling to the WTO's Appellate Body ("Body"). Antigua filed a cross-appeal shortly thereafter, and both countries made oral arguments before the Body. In April 2005, the Body issued a report that generally upheld the Panel's findings. It affirmed that the United States had committed to free trade in online gambling services and ruled that the three federal laws violated these commitments (although it did not refer to other state and federal laws that Antigua had sought to include). It also ruled that the United States, which maintained that these trade restrictions were necessary to promote moral goals, had not met the criteria of the "moral defense" permitted by GATS Article XIV under certain conditions. (This defense, for example, is invoked by some countries with large Muslim populations to restrict trade in alcoholic beverages.) The Body found that the federal laws were necessary to protect public morals or maintain public order, but the United States had not met the

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<sup>8</sup> All findings in this and the following two paragraphs are from WTO (2008a).

“chapeau” condition that regulations not discriminate between countries, noting that some U.S. companies are allowed to offer internet gambling services by accepting online wagers on horseracing.<sup>9</sup>

A WTO Arbitrator determined that a deadline of April 2006 would give the United States enough time to change its laws to comply with its commitments. The United States did not alter the laws in question by that deadline, but did issue a status report stating that its current laws prohibit the interstate transmission of bets and wagers; that it was investigating possible violations of these laws by U.S. companies; and that, in light of this, it was in compliance with the WTO’s rulings (i.e., it was able to successfully meet the chapeau condition of a moral defense). Antigua held that the United States was not observing the Body’s ruling and requested the establishment of a Compliance Panel. In March 2007 the Compliance Panel ruled in favor of Antigua.

In May 2007, the United States responded by invoking procedures under GATS Article XXI to modify its schedule of commitments, specifically excluding online gambling from its recreational services commitments. This is the first time a WTO member has withdrawn a commitment in response to a WTO ruling (*Gambling 911.com* n.d.). A condition of withdrawing from a GATS commitment is that the withdrawing country must compensate any affected WTO members, and after the United States’ announcement, Australia, Canada, Costa Rica, the European Union (EU), India, Japan and Macao all filed claims for compensation, arguing that they would be negatively impacted by the modification (*Associated Press* 2007). The United States negotiated settlements with Australia, Canada, the EU, and Japan, making commitments to maintain liberalized markets in the following U.S. industries: postal services, research and development services, technical testing services, and warehousing (*Online Casino City* 2008). Negotiations with Costa Rica, India, and Macao are ongoing.

In 2007, Antigua requested permission to retaliate against the United States by suspending some of its obligations under the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) (WTO 2008a). Antigua asked for the right to suspend \$3.4 billion worth of U.S. intellectual property (IP) rights (which comprise copyrights, patents, and trademarks)

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<sup>9</sup> “We find . . . that the Wire Act, Travel Act, and IGBA . . . satisfy the ‘necessity’ requirement [under Article XIV] . . . but [the United States] has not shown, in the light of the IHA, that the prohibitions embodied in these measures are applied to both foreign and domestic service suppliers of remote betting services for horseracing.”

annually, arguing that this was the value of Antigua-United States online gambling services trade that would have taken place had the United States complied with the initial WTO ruling (Kanter and Rivlin 2007). The United States challenged Antigua's estimate, claiming the true value would have been \$500,000. The WTO agreed to authorize the suspension and settled on a figure of \$21 million annually, their counterfactual estimate of Antigua's average 2001-2006 annual revenues from horseracing gambling services exports to the United States, adjusted for the impact of competing suppliers and for developments in US demand (WTO 2008a).<sup>10</sup> Antigua's domestic laws currently provide IP protections in accordance with TRIPS protocols, and at the time of writing legislation that would allow the suspension of IP rights held by U.S. firms has not yet been introduced (Antigua and Barbuda Ministry of Legal Affairs n.d.).

## **Consequences of Trade Commitments**

The Office of the United States Trade Representative (USTR) argues that it never intended its original GATS commitment to cover online gambling services, referring to their inclusion as an “unintended consequence of imprecision” in the 1994 draft (Office of USTR 2007). The United States made this point forcefully before the WTO Panel, arguing that it would have been “incomprehensible” for the United States to make this commitment, “given the over-riding policy concerns surrounding these services, which are re-

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<sup>10</sup>The WTO used two methods to estimate the average annual revenue loss for Antigua caused by US measures: data (provided by the private gambling consulting group Global Betting and Gaming Consultants) on the difference between Antigua's total remote gambling revenues in 2001 and in 2002-2006, which yielded a figure of \$304 million, and data (provided by seven publicly-listed companies) on remote gambling firms' average revenues per employee, multiplied by the difference between the number of such employees in Antigua in 2001 and in 2002-2006, which yielded a figure of \$196 million. The WTO adjusted these figures based on the almost 50-percent decline from 2001-2006 in Antigua's contribution to the Central American, South American, and Caribbean region's share of the global remote gambling market, resulting in figures of \$164 million and \$128 million. In restricting its award to only the share of revenue from gambling on horseracing, the WTO relied on the fact that horseracing had an average 11-percent share in all gambling activities from 2001-2006, yielding adjusted figures of \$18 million and \$14 million, and to account for the possible growth in the horseracing segment of the US remote gambling market in the absence of US measures, the WTO applied the 5-percent average annual growth rate from 2001-2006 in net receipts in the horseracing segment of the non-remote gambling market, yielding final figures of \$23 million and \$18 million for Antigua's average annual revenue losses. The WTO then took the average of these numbers and rounded up to the nearest million.



flected in the extremely strict limitations and regulations of these services” (Raghavan 2004).

The WTO Panel conceded this point, acknowledging that “the [U.S.] legislation at issue in this dispute predates by decades, not only the GATS itself, but even the notion of ‘trade in services.’ We have therefore some sympathy with the United States’ point in this regard.” But the Panel continued:

The scope of a specific commitment cannot depend upon what a Member intended or did not intend to do at the time of the negotiations. The purpose of treaty interpretation... is to ascertain the common intentions of the parties. These common intentions cannot be ascertained on the basis of subjective and unilaterally determined ‘expectations’ of one of the parties to a treaty... There are no provisions in the WTO Agreement that would allow a Member’s intentions to be probed and determined, except as reflected in the treaty language.<sup>11</sup>

The WTO’s decision underscores the general point that trade commitments can have unpredictable consequences. International trade agreements inherently impact national sovereignty inasmuch as signatories agree to choose only policies that do not reduce market access from negotiated levels (Bagwell and Staiger 2001, 545). This can affect regulatory flexibility in a wide array of behind-the-border policy areas, including import licensing procedures, customs valuation, sanitary and phytosanitary measures, and labor and environmental standards (Srinivasan 2002, 5). Trade agreements are incomplete contracts in that they cannot anticipate all future conditions, so industry trends, technological changes, exchange rate shocks, political realignments, or other contingencies can leave signatories with limited policy options (Mahlstein and Schropp 2007, 1).<sup>12</sup> Governments that make trade commitments freely accept these risks in exchange for anticipated market access gains and other benefits. However, the tension between national regulatory efforts and international trade agreements has surfaced repeatedly, in the EU’s ban on U.S. exports of hormone-treated beef (WTO 1997a), the United States’ ban on certain shrimp imports stemming from its 1973 Endangered Species Act (WTO 1998), and numerous other disputes.

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<sup>11</sup> Quoted in Raghavan 2004.

<sup>12</sup> Trade agreements can also create legitimacy problems if governments are perceived to be putting foreign obligations ahead of domestic ones; see the discussion of Argentina’s 2001 economic crisis in Rodrik, “Feasible Globalizations,” (2002), 15-6.

Trade in services agreements may involve unique uncertainties and risks, as developments in services can be especially difficult to predict. Services are intangible, non-storable, subject to rapid innovation, and are deliverable not only through cross-border transactions but also through the movement of consumers (consumption abroad), firms (commercial presence), and labor (temporary movement of people). Additionally, many research agencies are only now developing a robust set of trade-in-services statistics and analyses. The risks inherent in services trade commitments were emphasized in 1998 by former WTO Director General Renato Ruggiero, who argued that the GATS extends “into areas never before recognized as trade policy” (Ruggiero 1998). Countries try to anticipate future developments when making services trade commitments, but even the United States with its expertise and resources did not predict when it agreed to free trade in recreational services that this might one day be interpreted to include online gambling (a service that did not exist in 1994 when such commitments were scheduled).

There are ways to deal with the risk of unintended consequences. Many trade agreements have provisions allowing signatories to renegotiate or rebalance commitments, such as GATS Article XXI, invoked by the United States in the online gambling dispute, which lets countries compensate for the modification or withdrawal of existing market access commitments by making new ones. Trade agreements can also incorporate emergency safeguard measures: escape clauses that exempt specific products from liberalization commitments in order to provide temporary relief to domestic industries that are seriously and unexpectedly harmed. Article XIX of the General Agreement on Tariffs and Trade (GATT) regulates emergency safeguard measures for goods, and GATS Article X calls for discussions about similar safeguards for services. (Clogstoun, Trewin, and Bosworth 2006)<sup>13</sup> Safeguards can provide policy flexibility and increase domestic political support for liberalization agreements; it is plausible that the promise of eventual services safeguard measures helped countries make more and deeper services commitments in the Uruguay Round than they would have done otherwise (Sauvé 2002, 314). But safety valves can impede liberalization and limit the impact of trade agreements, as many of the benefits of liberalization come from credibly locking in policies and establishing high barriers to future backpedaling. Even trade commitments that go no further than confirming on-the-ground levels of liberalization can encourage investment when investors know that the rules are no longer subject to an-

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<sup>13</sup> Originally there was a 1997 target date for the establishment of such provisions, but in the absence of agreement that deadline has been repeatedly extended.

nual legislative renewal or other political conditions. The Antigua-United States dispute illustrates the balancing act demanded in international trade agreements: liberalization requires that countries be discouraged from unilaterally altering or withdrawing from commitments just because unpopular consequences arise, but countries are less likely to make commitments in the first place if it is too costly to deal with unanticipated online gambling-like developments.

## **Intellectual Property Rights and Cross-Retaliation**

The WTO generally grants aggrieved countries the right to suspend concessions and other obligations when partners violate their trade commitments, but these remedies are usually narrow, specific adjustments to bilateral trade, aimed at prohibiting an amount of offending-country exports equal in value to the damage caused by the offense (often through the imposition of *ad valorem* tariffs) (Chang 2004). In Article 22.3 of its Dispute Settlement Understanding, the WTO states that suspensions should be confined to the same sector where the violation occurred if possible (WTO n.d.). However, when no same-sector retaliation options would provide adequate compensation, the WTO has been willing to authorize cross-retaliation. Antigua successfully argued that raising duties on U.S. services imports would harm its economy without significantly affecting the United States. About 49 percent of Antigua's total goods and services imports come from the United States, but this amounts to less than 0.02 percent of total U.S. exports (Basheer 2007, 1).

TRIPS-based cross-retaliation was authorized by the WTO once before. In an Ecuador-EU dispute over bananas, the WTO gave Ecuador permission to suspend \$202 million annually in IP rights held by EU firms (WTO 1997b). Ecuador used this leverage to resolve the dispute in 2001, before enacting suspensions, on terms that incorporated many of its core demands (Smith 2006). Additionally, in 2005 the WTO Appellate Body ruled in favor of Brazil in a dispute with the United States over cotton, and Brazil has requested the right to suspend IP obligations in retaliation, arguing that increasing duties on U.S. goods imports would create inflation and harm industries in Brazil (WTO 2008b). At the time of writing, a WTO Arbitrator is preparing to rule on Brazil's request to impose annual retaliation of \$2.3 billion and a one-time retaliation of \$350 million in the withdrawal of IP rights and services commitments, equal to Brazil's estimate of the world-

wide impact of U.S. cotton subsidies (Wasson 2009).<sup>14</sup> Ironically, cross-retaliation originated as a way to protect the interests of developed countries, who wanted the ability to penalize developing countries that violated IP rights (Bassheer 2007, 24). IP-based retaliation would have limited effectiveness in such cases because developing countries produce little IP, so developed countries sought means of imposing tariffs on other goods and services exports from offenders (Basheer 2007, 4).

No country has actually suspended IP rights in accordance with a WTO ruling, so the online gambling dispute is in uncharted territory. Antigua could ignore U.S. copyrights on software, movies, and music owned by U.S. companies, and sell up to \$21 million worth of these media annually in domestic markets.<sup>15</sup> Antigua could also grant compulsory licenses and produce U.S.-patented products such as pharmaceuticals. However, while it is inexpensive to reproduce most copyrighted materials, many patented goods need to be manufactured, and Antigua's potential gains from patent suspension are limited by its lack of capacity to produce goods such as pharmaceuticals. And getting rid of trademarks, which identify the producer of a product and inform consumers where to seek recourse if the product fails, could erode the quality and safety of consumer goods (Fink and Smarzynska 2002, 404).

It is doubtful that suspending U.S. copyrights could increase domestic retail sales of U.S. copyrighted goods in Antigua by \$21 million annually, as this would require average new expenditures of \$300 per person in a country with a GDP PPP per capita of \$17,000 (CIA 2008). Antigua might consider exporting to reach the permitted level of retaliation, but the WTO Panel in the Ecuador-EU case noted that even when IP rights are suspended by one country, other WTO members are still obligated to follow TRIPS with respect to their imports (WTO 1997b). However, Antigua could export goods to countries where IP protections are not in place; for example, Antigua could theoretically suspend patents for HIV / AIDS medicines, manufacture

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<sup>14</sup> Notably, Brazil is arguing that the size and form of its cross-retaliation should be governed by the Agreement on Subsidies and Countervailing Measures, and not the Dispute Settlement Understanding. The former has vaguer language (countermeasures need only be "appropriate" and "commensurate with the degree and nature" of violations) whereas the latter requires stronger proof that same-sector retaliation is not practicable or effective. If Brazil's interpretation is upheld, it may lower the hurdles for cross-retaliation in future disputes.

<sup>15</sup> Palmer (2008) asks, "Would you go into a store [in Antigua] and see a 'real' version of Harry Potter for \$14.95 and a packaged, legally pirated copy for \$9.95 or even \$4.95? Would the legal pirates experience so much competition from each other that the price would drop to just enough money to cover the cost of the disc, duplication, distribution and retail profit, say \$3.00?"

them, and export them to countries where they are not under patent (Ruse-Khan 2008, 6).

It would be difficult to manage the suspension of IP rights to meet any specific monetary target. For many goods and services, there is no robust method for estimating the value added purely by intellectual content, so the exact value of any act of IP suspension by Antigua could be subject to challenge. In different contexts IP is valued based on the cost of research and development inputs, the anticipated future revenue streams derived from ownership of the IP right, or market prices for similar IP in third-party transactions, but these numbers can be subjective and highly variable (Hoi 2001). (IP-producing companies measure their performance in part by how much profit and revenue they can generate from a given amount of IP.) One of the guiding principles of the WTO is that the negative effect of retaliation on countries must be equivalent to the harm caused by their non-compliance, so difficulties in quantifying the impact could make IP-based retaliation unworkable (WTO n.d.).

Other considerations include the fact that Antigua is obligated to respect U.S. IP rights under separate agreements. The Caribbean Basin Economic Recovery Act (CBERA) gives Antigua preferential access to U.S. markets, but grants the United States the right to alter the terms of the initiative unilaterally and without consequence if Antigua disregards U.S. IP rights.<sup>16</sup> In 2007 only 1.6 percent of Antigua's exports to the United States entered under CBERA preferences, but the potential loss of preferential access to U.S. markets is nevertheless a disincentive to retaliation (USITC 2008, 2-21). The Berne Convention and the Paris Convention are other multilateral agreements that provide IP protections, and the issue of whether WTO rulings supersede these treaties is complicated.<sup>17</sup> Finally, the suspension of IP obli-

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<sup>16</sup> CBERA was enacted August 15, 1983, as Pub. L. 98-67, Title II; 97 Stat. 384, 19 U.S.C. 2701 et seq., and became effective January 1, 1984 (Proclamation No. 5133, 48 Fed. Reg. 54453, November 30, 1983).

<sup>17</sup> According to Subramanian and Watal, (2000), 411: "Two observations are relevant here. First, Article 2.2 of TRIPS, which upholds the existing obligations that WTO Members have to each other under other IPR conventions and treaties, does not extend to the dispute settlement provisions of TRIPS. Second, to the extent that the WTO's dispute settlement rules provide for or allow TRIPS commitments to be withdrawn, the possibility of conflict always existed . . . [This] conflict would, under customary rules of interpretation of international law as laid out in the 1969 Vienna Convention on the Law of Treaties, have to be decided in favor of TRIPS, which is the later treaty." On the other hand, see Basheer, (2007), 34: "[Article 2.2] states that nothing in TRIPS shall derogate from obligations of members states under either Paris or Berne. In other words, obligations under Paris and Berne are to subsist independently even after the advent of TRIPS... Illustratively, Article *obis* of the Berne Convention [which confers "moral rights" on authors of IP] has not made it into TRIPS. In so far as provisions such as Article *obis* are concerned, the Berne provisions continue to subsist."

gations may harm Antigua's reputation and discourage foreign investment if companies fear their intellectual assets will not be protected. Antigua had \$207 million in foreign direct investment inflows in 2006, which accounted for 46 percent of its gross fixed capital formation (UNCTAD 2007).

These considerations may persuade Antigua not to suspend IP rights. But the WTO aims to give all member countries effective recourse in trade disputes, and IP suspension is one of the few methods by which small developing countries can inflict economic damage on large developed countries. The WTO has faced criticism in the past for providing insufficient protections for developing countries in trade disputes in the face of information and resource asymmetries;<sup>18</sup> one study of GATT/WTO disputes found that 50 percent of the complaints brought by developing countries in the WTO resulted in the complainants gaining full concessions, while the figure for developed countries was 74 percent (Busch and Reinhart 2003).<sup>19</sup> More powerful retaliatory measures will not alter the fundamentals of enforcement, and suspending IP rights may be too costly or difficult for many countries, but the option of suspending IP rights can increase the leverage of developing countries in trade disputes and give IP-producing countries stronger incentives to change their policies if they are in violation of trade rules.<sup>20</sup>

As Antigua weighs the costs and benefits of retaliation, a final point is that a socially optimal IP regime balances the goals of protection and access. IP producers have incentives to stake out the maximum territory covered by their claims, using IP rights as legal weapons to collect royalties, establish monopolies, and block new market entrants. On the other hand, consumers and second-generation innovators have incentives to minimize IP protections, which lowers their costs and increases their access to new technologies even as it reduces compensation for first-generation research and

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<sup>18</sup> See Steinberg (2002). Also see UNCTAD (1999), 40: "the special and differential treatment which the Uruguay Round accorded [developing countries] has been inadequate . . . [and] insufficient human and financial resources and weak institutional capacities have restricted the ability of many developing countries to exploit the opportunities open to them under the WTO system . . ."

<sup>19</sup> However, developing countries might achieve even fewer concessions if they attempt to resolve disputes with developed countries through bilateral negotiations. For example, Peru won a 1999 sardine-labeling case against the E.U. using the WTO's dispute resolution process, while Vietnam, in a similar 2002 catfish-labeling case, was unable to successfully challenge the United States through bilateral means. (Vietnam was not a WTO member at the time.) Davis (2006).

<sup>20</sup> See Smith (2006).

development. Ideally, IP protections should be strong enough to encourage creators and let them recoup their investments, but not so strong as to inhibit fair access and further innovation. Antigua may agree with critics of TRIPS that the treaty's IP protections are too strong, and anticipate that the suspension of IP rights will stimulate domestic innovation (Yu 2006). For example, nascent Antiguan industries such as pharmaceuticals or agriculture could use valuable inputs, such as patented technology or copyrighted scientific material, at lower costs in the absence of IP protections (Yu 2006). Firms, however, might be reluctant to invest in new, suspension-based capacities given that IP rights could be restored as soon as the United States enters into compliance. And harm done to legal and social norms of IP protection may discourage creative industries, and perhaps damage the rule of law, in Antigua.

## **Conclusion**

This dispute has captured the attention of U.S. movie, music, software, and pharmaceutical industries, which have a stake in preventing a precedent-setting act of IP rights suspension (Rivlin 2007). The United States produces and exports a large amount of IP—in 2005, U.S. firms received \$57.4 billion in IP licensing fees alone (NSB 2008)—and IP-producing firms may pressure the United States to negotiate a settlement with Antigua, or to pass legislation that legalizes online gambling or prohibits online horseracing wagers and thereby brings the United States into compliance with the WTO's rulings. In the Ecuador-EU dispute, after Ecuador won the right to suspend IP rights, the European Confederation of Spirits Producers immediately began lobbying EU officials to settle with Ecuador in order to prevent the enactment of retaliatory measures (Smith 2006).

The United States continues to face challenges in preventing its citizens from gambling online. Virtual betting parlors are available to anyone with a computer and a credit card. In 2005, there were at least 2,300 internet gambling websites generating \$12 billion in worldwide revenues, with at least \$6 billion of that originating in the United States (House Committee on the Judiciary 2006). The lack of regulation and oversight leaves players vulnerable to abuse, as in recent cheating scandals at AbsolutePoker and UltimateBet (Gaul 2008a). But in some respects online gambling exhibits behavior typical of legitimate industries: the internet facilitates information exchanges that drive dishonest casinos out of business, and online gambling websites compete on the basis of reputation, availability of customer service hotlines, variety of games offered, and other features (Gambling

Forum n.d.). The FAQ page of one popular online casino is candid about the industry's strange legal status: "Is it legal to bet online? It depends a great deal on where you are living. There are no records of anyone getting into trouble because they have gambled online even though it was illegal to do so in the state or country where they live " (Gambling Forum n.d.).

The Antigua-United States online gambling dispute resulted from a combination of U.S. legislative processes that struggled to balance competing interests and U.S. services trade commitments made in a sector that developed unexpectedly. As the online gambling industry grew, U.S. laws governing online gambling were stuck in a state of ambiguity, and in the eyes of the WTO the United States failed to resolve this ambiguity in a way that complied with its trade commitments. But suspending IP rights is a thorny means of retaliation. If Antigua chooses to do so, it may set a precedent that provides small countries with useful leverage in trade disputes; but the difficulties of implementation and the harm done to Antigua's reputation might overwhelm and outlast the economic benefits.



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