

## **Money Managers: U.S. Will Enforce the PATRIOT Act**

**To enforce the USA PATRIOT Act, the U.S. Attorney General made an example of PayPal by asking the company to relinquish gambling revenue. Further actions will likely occur, so money managers should take the regulations seriously.**

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**Event:** On 28 March 2003, eBay said it received a letter from the U.S. Attorney for the Eastern District of Missouri accusing its PayPal subsidiary of violating the USA PATRIOT Act. The law requires banks and securities firms to take steps to prevent terrorists from easily transferring money. According to eBay, the U.S. Attorney's letter offered a plan that would enable the company to settle all charges if PayPal turns over earnings and interest from online gambling for the nine-month period ending 31 July 2002. In August 2002, PayPal agreed to restrict online gambling merchants from using its transaction system and paid a \$200,000 penalty to New York state. After eBay bought PayPal in October 2002, PayPal stopped processing payments for online gambling companies.

**First Take:** The PayPal case marks the second time the U.S. government announced enforcement of the PATRIOT Act by levying charges against a nonbank money transmitter. In December 2002, New York state officials said that First Data's unit Western Union Financial Services agreed to pay \$8 million to settle claims it had failed to file suspicious activity reports to detect money laundering. If PayPal relinquishes earnings and interest from online gaming, it could pay out \$200,000 to \$15 million (although the exact amount is disputed). In 2002, PayPal received 6 percent of its revenue from online gambling, or \$10 million to \$15 million.

The USA PATRIOT Act stipulates that if enterprises manage or move money (for example, pawnshops and banks), they must perform due diligence in checking customers' identities before granting them accounts. Banks and other money-movers are legally responsible and are fined if authorities discover that accounts are used to launder money and that the account holder was not checked carefully when the account was opened. When PayPal opens accounts for customers, it does not ask them whether they intend to use their accounts for online gaming or any other activities.

The PayPal and Western Union incidents should alert money managers that they will have to take these regulations seriously. Gartner expects more enforcement of the regulations by 2H03. Banks and other enterprises managing money should invest in applications that help them authenticate customer identities when opening accounts. The action taken by the U.S. Attorney against PayPal will likely give this growing market a further boost. If PayPal must pay steep fines to the United States, it will likely hurt eBay's balance sheet.

**Analytical Source:** Avivah Litan, Gartner Research

## **Recommended Reading and Related Research**

### **Gartner**

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- “PayPal Acquisition Fits eBay Despite Challenges” — eBay would likely benefit from a purchase of PayPal even though it would inherit the payment service’s legal challenges. **By Kenneth Kerr and Avivah Litan**
- “Online Person-to-Person Payments Move Into the Mainstream” — Gartner research shows growing consumer acceptance of online payment systems — and a strong lead for PayPal. **By Avivah Litan**

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