

## **EXECUTIVE SUMMARY**

### **A Virtual Fortune: Consumer Protection for Banking and Consumer Fraud in Virtual Worlds**

By the Public Interest Advocacy Centre

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Virtual worlds are sometimes described as “massively multiplayer games” (MMGs) or “massively multiplayer online role-playing games” (MMPORGs). MMGs leverage the scale of the internet to involve thousands of people at once in a shared gaming experience. Some virtual worlds offer a fantasy world wherein players must engage in quests to achieve power and wealth, such as Entropia Universe, EVE Online, and World of Warcraft. Other virtual worlds give its users the opportunity to create, innovate and monetize their creations in these worlds. Such worlds do not have a goal and rather provides a platform for users to explore and create. MMGs are very popular, engaging more than 100 million gamers per month and generating more than \$4 billion per year in subscription revenue for game companies. To many players of these games, their virtual experiences are just as “real” as real-world experiences. Virtual worlds offer a form of entertainment. Sociologists and psychologists have studied virtual worlds with great interest and it is generally accepted that the virtual world “avatar” forms part of the real-world individual's identity and acts as an extension of real individuals.

Many virtual worlds have their own in-world economy that is based on an in-world virtual currency. Avatars often play the role of consumer and entrepreneur within virtual worlds. The type and amount of economic activity varies according to the rules of the virtual world and the degree to which economic activity is encouraged by the virtual world operators. Players can participate in economic activity in-world by participating in activities that reward them with in-world currency, trading items or by converting real-world currency into virtual currency through a currency exchange. Other worlds encourage economic activity by encouraging its users to create and design items or services in these virtual worlds that they could then monetize by selling to other users. Some worlds allow virtual world currency to be exchanged to real-world currency. Thus, virtual worlds beget own virtual economies that have ties to the real world economy. A European survey conducted in 2007 with virtual world users found that 70% of respondents conducted commercial activities in a virtual world.

As virtual economies grow, some players have seized opportunities to earn money through actions that would be characterized as fraud in the real-world – by stealing, duping other players, and running Ponzi schemes. In virtual environments, users maintain a cloak of

anonymity and economic transactions are barely regulated if at all and thus the potential for fraud is high. Virtual world players are soft targets for cybercriminals and a European survey indicated that 30% of users recently lost some form of virtual property through fraud.

This paper discusses examples of economic fraud conducted in virtual worlds that have resulted in a loss to consumers in these virtual worlds. Notably, virtual world operators have in some cases stated that these fraudulent actions are merely “part of the game”, denying all responsibility and liability for these actions and refusing to compensate players who have lost money to these schemes. Virtual world consumers are often unable to seek redress or compensation for their loss.

Some virtual worlds, such as Entropia Universe and EVE Online, host user-run banks. There have been examples of bank runs in EVE Online valued at \$150,000 USD and \$5,100 USD but according to the game operator, this was part of game play so no compensation or redress was offered to victims. A bank run in Second Life valued at \$750,000 USD of lost money resulted in a change of Second Life policies. Individuals must demonstrate that they have a real-world bank charter in order to operate a bank or financial institution in Second Life. Second Life also offered a securities market, though one notable stock exchange closed due to pervasive problems with false information and rampant speculation. There have been reports of investment fraud in Second Life, EVE Online and Entropia Universe. In EVE Online and Entropia, the virtual world operators state that these practices are part of gameplay and have not punished the offending player or provided redress for victims.

Some virtual worlds prohibit the trade of virtual currency to real world currency in efforts to keep the virtual economy contained. One such world is World of Warcraft and yet the controversial practice of real money trading persists with reports of gold farming by low-wage workers in China.

Virtual worlds can also be used as a vehicle for real-world crimes. For example, payment system chargeback fraud is more prevalent for transactions involving digital goods than for physical goods. Security experts have noted a large growth in the malware and phishing attempts directed at virtual worlds which could result in identity theft. Fraudsters are also increasingly attracted to virtual worlds, where there are numerous ways they can attempt to steal private data for fraud. There have been reported examples of real world arrests and convictions of individuals who committed real world crimes such as assault, extortion, or in one extreme case, murder, in order to personally gain virtual assets, be it virtual goods or virtual currencies.

Virtual world assets have also been used for fraudulent activities in the real world. For example, law enforcement agencies have noticed that virtual worlds are used for money laundering. Virtual worlds have few if any means of monitoring financial activity, sparse due diligence, and rarely are there mandated forms or reports to complete for moving money. Virtual worlds have thus attracted scrutiny by real-world regulators and legal scholars and much discussion has surfaced regarding whether real-world laws should apply to virtual worlds. Given that individuals view the avatar as a virtual extension of themselves, this begs the question of whether real-

world rights should extend to the avatar and whether traditional notions of property rights and consumer protection should apply to virtual avatars participating in virtual economies.

Efforts to set up in-world justice systems for virtual world fraud have not been successful and where virtual consumers lose money in a virtual world due to fraud, they are unable to find compensation for their losses, as the harshest sanction for a virtual world operator is to banish the offending player from the virtual world. The operator will not issue refunds. In some cases, virtual world players have turned to real world authorities for assistance. Some countries such as the Netherlands have seen criminal convictions flowing from virtual fraud, but law enforcement agencies are still learning about virtual worlds.

Virtual world operators use the End-User License Agreement (EULA) or Terms of Service to govern over the players of the game. The EULA is a non-negotiable instrument to which consumers must agree in order to play and establishes the virtual world operator's unequivocal right to take unilateral actions in-world and with player accounts. Consumers should be made more aware of the risks to their in-world assets and property. Users may not be so aware that it is a possibility that providers may permanently delete or confiscate assets without warning, thus users should be aware of this fact and take it into account when valuing assets. Some virtual world EULAs also attempt to limit the operator's liability, stipulate mandatory arbitration or jurisdiction in their terms. The enforceability of these terms in real world courts have been questioned and in one case in the United States, the court ruled that a mandatory arbitration term in the Linden Lab Terms of Service was unconscionable and thus unenforceable.

Real world case law is not yet helpful as it remains unclear what the legal status and rights of virtual world users and providers are in relation to property rights and contractual obligations. At the moment, there does not appear to be any Canadian case law pertaining to virtual worlds. If a consumer turned to real-world courts in an effort to assert rights over virtual assets in a virtual world or to seek damages for a wrong conducted in a virtual world, there would be several complicated legal issues at play. Where an in-game fraud was perpetrated by a third party that is not the world operator, such as another player, the consumer may not be able to ascertain the real-world identity of the perpetrator in order to seek justice in real-world courts. For example, questions of jurisdiction and the applicability of certain terms in the EULA such as mandatory arbitration clauses may need to be resolved before the merit of the heart of the dispute can be examined. Resolving these questions will likely take years to resolve in court. The experience of American cases dealing with virtual world disputes shows that commenced actions have resulted in settlements. Unfortunately, this does not advance legal precedent or provide greater clarity for consumers wishing to seek justice through real-world courts.

Real-world regulators around the world have been examining virtual world economies and contemplating whether real-world regulation should be applied to financial transactions conducted in-world, for example, applying securities and payments regulations with a view to providing greater consumer protection to virtual world users. These discussions are only in nascent stages and should be monitored to ensure that consumer protection is at the forefront.

Experts suggest that the future of virtual worlds has not yet been realized and are only now in the startup phase with a number of isolated virtual worlds. Experts predict that virtual worlds will go mainstream as kids and tweens are participating in virtual worlds that target them.

As virtual worlds continue growing as economic spaces for consumer participation, consumer protection will be of utmost importance. Virtual world experiences are now blending into social networking websites and other areas of electronic commerce. Further research should be done on specific consumer issues, such as virtual currency as legal tender, liability for economic transactions in virtual worlds, monitoring consumer dispute resolution processes in-world and with the virtual world operator, and avatar privacy.