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Contracts can't be
completely one-sided.

What Is a Contract?

Contracts are the legal backbone of modern commercial life. Because people deal with contracts so regularly, from employment contracts to credit card contracts, their intuitive idea of what a contract is—an exchange of promises that the legal system will enforce—is more or less accurate.

There are two basic requirements that govern the process of contract formation:

- There must be *manifestations of assent* by both parties. It's not strictly accurate to say that each side has to agree to the contract; what matters is what they communicate. Keeping your fingers crossed while saying you'll agree to a contract won't get you off the hook; if a reasonable person would think you'd indicated your intent to be legally bound by the contract, you will be legally bound by it. Similarly, you will be bound by it whether you negotiated the deal individually or accepted a standard set of terms (such as those that come shrink-wrapped with new software).
- There must be *consideration*: Both sides must give up something of value. Consideration may be money, but it may also be the performance of a service, the value manifested in agreeing not to do something, or even the proverbial "peppercorn," something whose only purpose is to be worth slightly more than nothing. Contracts can't be completely one-sided: at least a nominal exchange must take place.

How Does Contract Law Work?

In order to make the process of determining whether there really has been a mutual manifestation of assent simpler, the law imposes various requirements on the *formalities* of making contracts:

- Contrary to folk wisdom, many oral contracts are legally binding.
- However, because it is often difficult to prove the existence of an oral contract, the law also requires that certain "important" contracts be in writing and signed. Typically these include contracts involving real estate and those that involve more than a limited amount of money or time. These requirements give people a strong incentive to write down their contracts.
- The law recognizes *electronic signatures* as the legal equivalent of paper ones. Clicking "confirm" on a Web site can generate a binding contract.

In the U.S. and in many other countries, when one party to a contract fails to follow through on her commitment ("breaches" the contract), the other party's legal remedy is usually *expectation damages*. If Alice breaches a contract with Bob, then a court will order Alice to pay Bob enough money to make his as well off as he would have been if Alice had kept her end of the bargain. Alternatively, especially when it is hard to measure the actual value of Alice's performance, a court may order *specific performance*, meaning that it compels Alice to fulfill the promise she made in the contract.

Some other points about contract damages:

- Once Bob learns that Alice has breached the contract, he is under a *duty to mitigate damages* and act as he would if Alice weren't required to pay him back. If he behaves wastefully, Alice won't be liable for the excess damages he's run up.
- If Alice and Bob want, they can decide in advance what damages one of them should owe the other in case of a breach. A court will uphold such *liquidated damages* unless the amount specified is clearly disproportionate to the actual loss suffered by the innocent party.

The most complex part of contract law involves determining the conditions under which one party to a contract will be *excused* from carrying out her side of the bargain. These excuses are either exceptions to the general rule that contracts freely negotiated between parties will be binding on them or involve cases in which the negotiation didn't really work as intended. Examples include:

- *Impossibility*: When circumstances change so much that the "essential purpose" of the contract will be frustrated, no matter what the parties do, the law allows them both to walk away. For example, if Alice promises to build Bob a house on a tract of land that falls into the ocean in an earthquake, the law won't try to figure out how much that house would have been worth.
- *No "meeting of the minds"*: If, despite their superficial agreement, the parties had completely different ideas in mind about the contract, a court may also agree to cancel it. The classic case involved a shipment that was to be delivered on a ship named "Peerless," but there were two different

ships with that name, and the parties had different ships in mind.

- *Duress*: If one side was unfairly forced into signing a contract, performance will be excused; you will not be held to a contract you signed with a gun to your head.
- *Illegality*: If you make a contract that calls for one side to act illegally, no court will enforce it. For instance, despite their name, “contract killings” are void as a matter of law.
- *Forbidden terms*: Most jurisdictions have laws that disallow certain kinds of contractual terms; these terms will simply be read out of a contract that contains them. For example, in the United States, insurance contracts are very heavily regulated: The maximum and minimum rates that insurers may charge are often set by state officials. Similarly, federal consumer-protection laws bar certain terms that credit card companies might otherwise put in their contracts.
- *Unconscionability*: If a contract is structured so as to overwhelmingly favor the interests of one party, a court may decline to enforce it. Unconscionable contracts are often created when one party is in a superior bargaining position, such as when the other party is bargaining for the purchase of necessary goods.

Contracts and Virtual Worlds

Virtual worlds are governed by contracts. When players subscribe to a game, they exchange a subscription fee for the right to play the game for a specified length of time. The contract that governs that agreement is usually referred to as the End User License Agreement (EULA) or the Terms of Service (ToS). These contracts give game companies control over players that goes beyond the control provided by the software.

They require players to promise to do or not to do certain things and to forego various legal rights as a condition of playing the game.

Among the legal issues that EULAs govern are:

- Intellectual property rights in game content, which players are often required to assign to game companies (see the Copyright and Trademark primers for more).
- Real-world property rights in virtual items, which players are often required to disclaim explicitly (see the Property primer for more).
- Rights to self-expression within the game world. EULAs generally provide that game companies may terminate the contract and ban a player from a virtual world—thus leaving a player “censored” by the game without legal recourse (see the Free Expression primer for more).


In light of their comprehensive control over so much of virtual world life, EULAs play an important role in enforcing both real-world law and the virtual laws imposed by the game designer. The appropriate scope of EULAs

continues to be a pressing issue for those interested in the regulation of virtual worlds. Some praise the way in which EULAs allow game designers to insulate games from the fantasy-ruining aspects of modern life and create genuinely “other” realities; others blame EULAs for what they see as severe power disparities within these realities, as a result of which players are at the mercy of designers.

Current questions for virtual world contract law, some of which have been debated at previous State of Play conferences, include:

- Might incentives, such as limitations of liability, be offered to game designers to get them to sign on to more player-friendly contract terms?
- Do EULAs provide game companies with truly unlimited power to seize player property, censor player speech, and control all aspects of the game?
- How much should contracts written by game companies be used to regulate relations between players? Should one user be able to bring a claim against another for disrupting game play by violating the terms of a EULA?
- Do EULAs improperly circumvent property law by requiring players to preemptively disclaim their rights to the content they generate?
- Can game companies effectively restrict property rights via EULAs that they otherwise appear to confer? If a company’s public statements regarding player property rights directly conflict with the terms of a game’s EULA, is the contract enforceable?

EULAs generally provide that game companies may terminate the contract and ban a player from a virtual world.



The *scope* of copyright law has expanded *significantly* in recent decades. Ideas themselves aren't copyrightable, only particular *expressions* of ideas are.

What Is Copyright?

Copyrights are sets of exclusive rights, granted for limited periods of time, that govern the ways in which particular material expressions of information may be used. Copyright law is largely dictated internationally by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), which sets standards for the length and process of conferment of copyrights, delineates which types of works are eligible for copyright protection, and limits national exceptions to the scope of copyright (such as fair use), and by the World Intellectual Property Organization (WIPO) Copyright Treaty, which penalizes the circumvention of technological barriers to copyright infringement.

The scope of copyright law has expanded significantly in recent decades:

- The *subject matter* of copyright, originally limited to written works, now includes many other tangible forms of expression. Songs, works of art, and films, among others, are now eligible for copyright, and TRIPS explicitly expands copyright protection to software.
- The *exclusive rights* conferred by copyright, originally limited to the right to make copies, now include a number of related rights: the right to distribute the work; the right to perform the work publicly; the right to display the work publicly; and the right to make *derivative works*—mixtures of copyrighted works and new creative elements.

How Does Copyright Law Work?

The basic rule of copyright is that the holder of a copyright in a work can sue anyone who makes a copy of it (or violates another exclusive right) without advance permission. The copier—called an *infringer*—will be liable to pay money damages to the copyright holder. In addition, the copyright holder can get an *injunction*—a court order telling the infringer to stop immediately or suffer severe consequences. The ability to sue unauthorized copiers enables business models in which authors sell copies (such as books and computer games on CD) and ones in which they sell the right to make derivative works (such as the movie rights to a book). There are also a number of very important limitations on copyright:

- Ideas by themselves aren't copyrightable; only particular *expressions* of ideas are. Had he lived today, Shakespeare could have copyrighted the text of *Romeo and Juliet*, but not the idea of star-crossed lovers.
- Purely factual information, such as phone numbers, can't be copyrighted.
- Copyright does not prohibit independent recreations: If you and I write very similar songs without hearing each other's version, neither of us is an infringer.
- A balancing test called *fair use* shields many uses of copyrighted material that would otherwise be considered infringing. Classic examples of fair use include quoting passages from a book in a review, copying a page from an old newspaper article as a classroom handout, and writing a parody of a song. There is no definitive list of uses that are or are not fair, only a set of four factors that courts balance:

- The "purpose and character of the use:" Works for nonprofit purposes are more likely to be considered fair.
- The "nature of the copyrighted work:" The smaller the investment of creativity in the original work, the more likely that a use of it will be considered fair.
- The amount of the work copied: Using small excerpts is more likely to be considered fair than copying an entire work.
- The effect of the use on the market for the work: Uses that don't compete with the original are more likely to be considered fair.

Why Do We Protect Copyrights?

It is usually said that the purpose of copyright law is to encourage creativity. The exclusive right allows authors to make money by selling copies of their work, which gives them a financial incentive to be creative and to share their creativity with the public. On the other hand, by giving one person the right to prevent copying and derivative works, copyright restricts the flow of information and may discourage subsequent creativity. Scholars often say that the goal of good copyright policy is to balance these concerns to maximize the amount of creativity that reaches the public.

Copyright and Virtual Worlds?

Speaking generally, possible copyright issues involving virtual worlds can be divided into three large groups:

- Copyrights in the game software itself.
- Copyrights in the creative elements contributed by the designer, such as the game's interface, its graphics, its story elements and text, and its music.
- Copyrights in the creative elements contributed to the world by the players, such as text they type, textures they upload, and digital objects they create.

The game designer almost always has a copyright in the game's software itself. At the most basic level, because it is copyright infringement to copy that software, game designers can make money by selling copies. As October 2003's theft of the source code to Half-Life 2 showed, the software itself can be extremely valuable. Other interesting legal issues arise when players try to set up their own game servers by reverse-engineering the behavior of the client: In 2002, Blizzard Entertainment used a copyright-like provision to sue a group of independent developers who created server software to mimic the functionality of its servers for playing Warcraft online.

Many virtual world developers want to use their copyright over creative elements as a way of prohibiting players from buying and selling virtual assets for real money. Companies that ban eBay sometimes argue that because they do not authorize such sales, anyone who buys a virtual item despite the company's prohibition is a copyright infringer. The copy involved, typically, would be the one made on the user's screen when she uses the virtual item she bought from another player on eBay. (These anti-eBay legal arguments can also be rooted in the terms of service that players must agree to in order to join a virtual world).

As for player copyrights in other creative elements, almost all virtual worlds give players techniques to express themselves, techniques that might be used to produce or insert copyrighted material. Whether a player types the lyrics of a copyrighted top-40 song while virtually talking to another player, uploads a texture she created herself at home, or makes a digital object that could only "exist" in the virtual world itself, all sorts of creative elements are possibly copyrighted. Major questions these copyrights raise include:


- If a player uploads a copyrighted work into, or creates an infringing derivative work within, a game without the copyright holder's permission, who is liable? The player? Other players who make copies of that work (perhaps just by playing the game)? The game company whose software is actually "making" the copies? If the latter, can a game manufacturer disclaim its liability by manipulating the terms of its EULA (for instance, by contractually obligating players not to infringe in-game)?

- Relatedly, can a game manufacturer craft its EULA so as to eliminate defenses (such as fair use) for players exporting copyrighted material out-of-game?
- Who should own the creative elements created by players: game designers, game players, or no one at all?
- Should players be able to sue other players for copyright infringement for in-game actions that involve creative elements? How should game designers respond?

In almost all of these questions, copyright law interacts with contract law in ways whose implications are not yet clear. Games' terms of service may require that players assign all copyrights in content they upload to the game designers and may also affect players' rights to sue for various claims, including copyright infringement.

One approach, employed in Linden Lab's Second Life, is to permit players to retain copyrights in any content they upload, while giving them tools to announce to other players the copyright status of that content. Players are able to use Creative Commons licenses to tag items as being either copyrighted or free for reuse and modification. The interaction between such legal elements and game software is a rich and complex topic.

The game designer almost always has a copyright in the game's software itself.



Free expression is one of the
cornerstones of liberal democracy.

What Is Free Expression?

“Free expression” is a term used to describe individuals’ rights to believe what they want and say what they want. Free expression is considered one of the cornerstones of liberal democracy, but the scope of the freedom of expression differs depending on the nature of the liberal democracy involved. It also differs dramatically between the real world and the virtual worlds.

Virtual Worlds and Free Expression

- A man carrying a high-powered machine gun shoots and kills his neighbors. No one arrests him, but several people shoot back while others cheer.
- A woman posts a sign supporting a political candidate on her front lawn, but her neighborhood has a rule banning all political messages.
- In response to serious overcrowding at a protest, the police transport some of the protesters to the next town over.
- A reporter breaks a story about minors engaging in sexual conversation with adults for money. The local authorities run him out of town and confiscate all of his property.

These are common scenarios arising in virtual worlds that give rise to questions of what the role of free speech law should be in such spaces—spaces that are privately owned and controlled. There are many kinds of possible speakers and speech in virtual worlds, and there are even situations in which protecting one speaker may impinge on another’s ability to speak freely.

First, the computer code on which games run is a kind of speech. Many courts in various countries have recognized that source code is a way in which programmers express their ideas to each other.

Games also contain speech by designers directed at players. The code produces story-like aspects of the game that may be speech in the same way that movies or novels are. Scholars have argued over whether the interactive nature of games makes the more or less speech-like. Jack Balkin has argued that games are akin to improvisational theater and deserve the same protections, but other scholars think that the expression “speech” involved in a player’s choosing to pull a virtual trigger is minimal.

The question of whether games should be considered protected speech has arisen most strikingly with respect to games that depict acts of violence, such as martial arts games and military simulations. Several states and cities in the U.S. have attempted, largely unsuccessfully, to restrict the sale of violent games to minors; other countries, such as Thailand and Germany, have strictly regulated such access.

Next, because virtual worlds often support rich chat systems and other in-game communications, speech issues also arise within games, based on the things players say there. When players role-play scenarios in a virtual world, their speech there may have meanings other than that which it would have in the real world. Sometimes shooting other players’ avatars is “part of the game;” sometimes lying to them and defaming them is too. Whether and when players should be punished for what they say in games raises difficult policy questions.

Almost all games have policies requiring some form of civility and reserve the right to kick out a player if they don’t like what the player says. But what if the offensive speech takes place outside of the game? And what if the speech wasn’t offensive to other players, but merely critical of the game designers? In a purely legal sense, because game companies aren’t governments, few restrictions apply to their actions in censoring players.

However, players have also appealed to the policy values underlying free expression to claim that game designers *ought* to encourage players to speak openly and to guarantee them freedom from reprisal for certain kinds of speech. Many large games have had rich internal debates about what kinds of speech should be allowed or not. Ted Castronova has proposed creating a legal status of “interration” (a pun on “incorporation”), in which virtual worlds that agree to protect players’ rights to free expression receive limited liability in other areas.


Cont...Free Expression Law Primer

Another special free speech problem that arises in virtual worlds involves intellectual property. Because copyright applies to work fixed in a tangible medium of expression, ordinary conversations in real life aren't copyrighted. But in a virtual world, everything is "written down" on the screen and on the game's servers. Who owns the copyrights in these words, and are there any free expression issues with the enforcement of these copyrights?

Nor are the free expression issues in virtual worlds confined to free *speech*. Some games deal with the slowdown associated with large crowds of players by randomly teleporting some of them to other parts of the world, a response that many players perceive as a restriction on free association.

Tal Zarsky has also claimed that in a virtual world, intrusions of privacy are possible on a scale unprecedented even on the World Wide Web, raising the question of whether expanded privacy protections are necessary for virtual worlds to protect the right of free association. Beth Noveck has suggested that the unique properties of virtual worlds are particularly conducive to fostering collective action as well as free expression by groups.

What if the speech wasn't offensive to other players, but merely critical of the game designers?



Property is a collection of closely associated rights, sometimes called a “bundle of sticks.”

What Is Property?

Property law, loosely put, is the body of law that governs people's rights in *things*.

The traditional breakdown of property is into three categories:

- Real property, which includes land and buildings. Think of "real estate."
- Personal property, which includes everything tangible that isn't real property. Cars, corn flakes, and computers are all examples of personal property.
- Intangible property, which includes everything that isn't real or personal property. Copyrights, trademarks, and other intellectual property fall into this category, as do stock and other securities.

How Does Property Law Work?

Paradigmatically, when something is "property," its owner has the exclusive right to use it. The legal system protects property owners when others interfere with that right. The actual legal work of property law typically involves two related functions:

- It sorts out competing claims to the same thing. If a dishonest developer sells the same house to two different families, the legal system will have to decide which of them is the true owner. Sometimes, as with intellectual property, the system needs to figure out whether a person has done the right sort of work to create a property right at all.

- It decides what an owner can do to enforce her property rights against others. A homeowner can have trespassers arrested, but not shoot them. A landlord can choose to whom to rent an apartment, but not in a racially discriminatory way.

Several important ideas given shape to the basic rules of property law:

- Property is not possession. Indeed, much of the point of property law is to help an owner to recover her property from a thief who has taken wrongful possession of it. Sometimes, however, property law conveys full property rights to those who have "mere" possession, such as the first person to claim property abandoned by its previous owner.
- Property is not a single right. Instead it's a collection of closely associated rights, sometimes called a "bundle of sticks." It may be possible to have some of these rights without having others. Some of these rights include:
 - The right to keep others from using the property.
 - The right to use the property yourself.
 - The right to sell the property, or to give it away.
- Different people may hold different sticks in the bundle. A landlord has a property right in a building, including the right to sell the property, but the tenants in that building also have property rights, including the right to use the property.
- Not all property rights can be reduced to contracts. While contracts are typically binding only on the people who agree to them, property rights are "good against the

world." You can have me arrested for trespassing on your land even if I've never signed a contract with you. Contracts often, however, adjust property rights or trade them: A landlord and tenant are altering their property rights when they sign a lease.

- There are often systems for keeping track of property. These include car title deeds, land registries, and stock certificates. These systems don't themselves constitute property, but they are an important kind of evidence about who owns what. Thus, a title deed may be considered conclusive proof of ownership unless someone can show that the deed itself was forged.

Why Does the Law Protect Property?

In John Locke's famous words, "As much land as a man tills, plants, improves, cultivates, and can use the product of, so much is his property. He by his labor does, as it were, enclose it from the commons." Locke's ideas about the value of property have stayed with us to this day.

Property rights are a way of meting out resources in a way that gives people incentives to put them to productive use. This view suggests that property rights should be assigned in a way that maximizes the overall social benefit from those uses. Locke's tiller is adding value to the land by cultivating it, so he should be given a property right to encourage his work.

Property rights are also a way to protect freedom and personal autonomy. In Lockean political theory, property rights give the individual a sphere that is safe from outside intrusion—particularly intrusion by an abusive government.

Virtual Worlds and Property

Many of the most perplexing questions about virtual worlds involve issues of property law. Game servers are generally the property of the game company. This would seem to imply that the game company always has a right to “take its ball and go home,” by shutting down the servers and ending the game. But many players are deeply attached to a game and often wish to keep playing. Some games, such as Meridian 59, have even survived the original company’s complete withdrawal, thanks to servers set up by others.

From virtual worlds to virtual saunas to the ability to play under a particular name, players acquire in-game resources that resemble all three kinds of property. The games’ software will certainly help them to exclude other players from using these resources. Does that mean that the law would or should step in to protect this ability, as well? Dan Hunter and Greg Lastowka have suggested that perhaps real-world law ought not be brought to bear to enforce in-game property rights.


Questions of players’ rights in virtual property are not only academic. Since players buy and sell virtual items for significant sums of real-world money, it matters a great deal to them whether they have a legally enforceable property right in these items. Such rights make it easier for them to safeguard their investments and to get restitution after a fraudulent trade. Chinese and Taiwanese courts and governing bodies have held that players do have property rights in in-game property, and have enforced those rights via both civil and criminal means.

The government of South Korea has left the explicit status of property rights in virtual worlds unclear, but has in many cases applied criminal sanctions to the theft of virtual property.


Many game companies disagree with the approach of these Asian governments: They consider the purchases of in-game goods out-of-game to be the equivalent of a black-market trade and would like to be able to ask courts to shut down these markets by ruling that players do not have property rights in virtual items.

If players do have property rights inside a virtual world, these rights might also be used to defend against cases of alleged censorship, in which players are ejected from games for behavior the game company deems anti-social. Since there is little protection against censorship by private parties, players might instead assert interference with a property right.

Even without involving the real-world legal system, there are interesting property-themed questions in virtual worlds. Virtual worlds are, in effect, conducting vast experiments in different property systems; various studies of virtual economies have pointed out ways in which design decisions have consequences for the property systems those decisions generate.



Virtual worlds are conducting vast experiments in different property systems.



Trademarks allow consumers to make quick, meaningful choices among competing products.

What Is a Trademark?

A trademark is the exclusive right to use a particular phrase or symbol in connection with selling goods or services. Unlike a brand, a trademark identifies the source of the goods. Consumers who see a trademark can be confident that it identifies goods that come from a source approved by the trademark holder and are prepared to quality standards set by the holder. Thus, trademarks allow consumers to rely on their prior experiences and make quick, meaningful choices among competing products and services. To businesses, trademarks are a way to make a name for themselves (often called “good will”) and to maintain repeat customers.

How Does Trademark Law Work?

The rules of trademark law are designed to ensure that consumers can rely upon a meaningful connection between a trademark and an approved source. Thus, the central rule of trademark law is that competitors cannot use the mark in a way that confuses consumers.

Other doctrines of trademark law surround this central rule and help it to operate sensibly:

- Trademark protection isn’t available for phrases that are merely descriptive. If one restaurant could trademark the word “hamburger,” consumers would have more trouble ordering a good hamburger, not less. The more imaginative (and thus less descriptive) the mark, the stronger the legal protection.
- Similarly, a trademark that consumers start using as a generic term for an entire class of goods (e.g. Kleenex for tissues) becomes ineligible for trademark protection.

- Trademark-type protection is available for any distinctive decoration, not just words and symbols. A particular color of insulation or a particular style of restaurant décor may stick in consumers’ minds just as much as a name or logo would.
- Trademark holders must exercise some degree of quality control over the connection between the mark and the goods it identifies. A trademark holder who issues a “naked license” to a third party to use the mark without exercising some quality control can lose the right altogether.
- Trademark holders can sue for anything that “dilutes” the suggestive power of a trademark or “tarnishes” it in consumers’ minds. These additional rights help trademark holders to build strong brand identities by preventing others from polluting the meaning of the trademark.
- It is legal for others to use the trademark “nominatively”—that is, to describe goods on which the trademark holder has used the trademark. This rule permits Coke to mention Pepsi by name when advertising the results of taste tests, or for us to do so here.
- Because the same trademark may be associated with different styles of goods in different countries, trademarks also give their holders some exclusive rights over the importation of trademarked goods. The chocolate bar called a “Milky Way” in the U.S. is not the same as the “Milky Way” sold in the U.K.; unrestricted cross-border candy flow might lead to that bane of trademark law, consumer confusion.

Trademark is part of a broader set of doctrines, known as *unfair competition*, that generally regulate false or misleading advertising by businesses.

Trademark Law and Virtual Worlds

The most obvious connection between trademarks and virtual worlds concerns the “commercialization” of virtual spaces. Advertising-sponsored games are nothing new: For years, Yahoo, MSN, and others have offered free browser-based games that come along with banner ads. Sometimes, the advertisers’ brands and trademarks are directly integrated into the game play.

However, in recent years, the scope of in-game advertising has expanded immensely with the popularization of virtual worlds in the vein of Second Life and There, which offer their players the opportunity to purchase branded “real-world” goods in-game. Such commercialization has not been without its opponents: When The Sims Online announced plans to include McDonalds stands in its virtual world in 2002, activists threatened virtual protests.

This gives rise to the question of whether trademarks in virtual worlds are desirable. How should the law treat trademarks placed on virtual goods? Do they constitute naked licenses? How would they be enforced against those wishing to copy and use the brands? Is their use to be considered commerce?

Another twist on the idea of a branded virtual world is the didactic branded world, one created to educate players about a particular topic. The entire game functions as a form of advertising and may, itself, be considered a trademark entitled to protection as such. For example, the U.S. Army has developed a free multiplayer action game, America’s Army, as a recruiting tool. In addition to providing gamers with a positive view of military service, the Army hopes to teach them about the actual conditions soldiers face and about the importance of


Cont...Trademark Law Primer

military teamwork and respect for the laws of war. The Army also uses virtual worlds extensively in training its own soldiers.


The names and logos of games are entitled to trademark. Which individual elements of games—character names and appearances, and virtual landscapes, for instance—are entitled to the same protection, and to what extent, is an area in which the law is still developing. Synergistic, trademark-driven marketing is also responsible for an increasing number of crossovers between the gaming and non-gaming worlds. Star Wars and Star Trek have launched dozens of games over the years, while in the other direction, many famous game franchises have become movies of their own, from Tomb Raider to Resident Evil.

Inside of virtual worlds, players are facing many of the challenges of building and maintaining stable reputations that trademark law was designed to handle. How to adapt trademark doctrines to virtual worlds—or to find appropriate virtual replacements for them—remains a wide-open question. Many games allow players to open their own shops, and to buy and sell virtual items. In Second Life, which has a particularly rich set of options for player-designed clothing, owning an outfit made by a known designer has the same cachet that it does in the real world.

Finally, the extensive secondary markets that have developed for virtual items, such as eBay and IGE, raise issues of trademark law. On the one hand, trademark law may be among the legal weapons that game companies could use to shut such markets down, especially if some of the supposed auctions for game items are fraudulent. On the other hand, consumers who buy and sell such items are eager for assurances of reliability from their trading partners. The exclusivity of reference that trademarks promise is one route to that reliability; so also are reputation systems (both inside and outside of games) and other techniques of gathering information about other players.



In recent years, the *scope* of in-game advertising has expanded immensely.



While it is likely that virtual worlds will remain PC-based in the near future, console developers are already working on bringing this phenomenon to different platforms.

Overview

Online games can be divided into four categories: Massively multiplayer online games (MMOGs), multiplayer games, casual games, and synthetic worlds.

Casual games are games which are generally free to play online and tend to be puzzle/board/trivia/card games, such as Mah Jong, chess, and some variations of poker. These games account for around 59 percent of the online games market. Another 9 percent of the online game market is made up of popular games such as Bejeweled and other Shockwave, Flash, and browser-based games. The advantage of playing these games on the computer is that you may play against people all over the world and it is generally easier to hide a window on your screen from your boss than it is to hide an entire set of Mah Jong tiles on your desk! Otherwise, there is very little difference from their real-world counterparts.

Multiplayer games are generally session-based games. These games can host only 16–64 players able to play together at a time, due to small server capacity. In a multiplayer game such as Quake, a group of players who wish to play together will sign on to a specific server at a specific time so they may interact in the Quake playspace. When they are done with their session, the playspace in which they had just played is no longer occupied by any players, and therefore no longer exists.

Additionally, multiplayer games introduce the idea of playing a character, or group of characters, unlike in casual games where players generally represent themselves. As such, a player controls his character from a first or third person point of view, rather than directly manipulating pieces or answering in a game.

Recently, casual games have started overlapping with character-driven multiplayer games; a good example is the popular Audition Online. Labeled as a multiplayer online casual game, Audition Online allows players to dance online with and against other players, as well as purchase virtual items in an online store using microtransactions (monetary transactions of only a few dollars).

MMOGs, like multiplayer games, have users taking on the role of a character who engages in gameplay, usually role-playing gaming. In addition to the role-play aspect, a virtual world is created, by game developers, in which the gameplay takes place. This virtual world is a persistent environment in which all elements of the world remain existent whether players are logged in or not. The very nature of an MMOG, with thousands of players playing at any given time, requires a fixed world to be available at all times to accommodate players in varying time zones and at different levels of the game.

These games have multiple large-capacity servers that can hold anywhere from a few hundred to several thousand players at full capacity. The largest of these games are running environments with thousands of players playing simultaneously, such as the U.S./European market game Runescape, boasting 225,000 players co-existing in a game. Reports of concurrent usage are even higher in the Asia/Pacific market, with Fantasy Westward Journey recording 1.3 million players concurrent, and Yulgang Online's steadily generating concurrent usage of 300,000.

Synthetic worlds, such as Second Life and Project Entropia, have become popular in recent years. While synthetic world is nearly synonymous with MMOGs, synthetic worlds tend to focus on social elements and user-generated content. Because there are little to no

game mechanics specifically built through which one can progress, users or "residents," as they're sometimes called, create their own entertainment, building, buying, and selling things, and just interacting with one another in the virtual environment. Additionally, these persistent virtual worlds provide an interesting backdrop for creating virtual storefronts and brand-building marketing opportunities.

The Market Today

According to the latest surveys by the Entertainment Software Association, 69 percent of all heads of households play computer or videogames. Of these, 44 percent of frequent gamers say they play games online. 58 percent of online gamers are male and 42 percent are female. Seven percent of these gamers play in persistent worlds (MMOGs or synthetic worlds).

Recent Past/Near Future

U.S./European: After the hubbub of 2004's high-profile launches of Everquest 2 and World of Warcraft, 2005 and 2006 proved to be quiet years for MMOG releases, with very few new product launches. Several worlds saw an increase in their populations and profiles with the mainstream media. Second Life welcomed its first corporate citizens, and World of Warcraft commercial spots showed up on cable TV channels.

To fill the void of 2006, expansions were the order of the day in many global markets, a trend which has carried into early 2007. Guild Wars, following their pay for content business model, released Nightfall in late 2006. Cross-region success World of Warcraft captured record sales in nearly all available markets with its first expansion, The Burning Crusade.

New product launches will take over the expansions' spot at the top of the charts in 2007. The recent launch of the super-license The Lord of the Rings Online™: Shadows of Angmar™ (Turbine) has met with critical acclaim, but it is too soon to tell how successful it has been. Several titles, including Age of Conan - Hyborian Adventures, Gods & Heroes, and Tabula Rasa are expected to arrive before the end of the year, and long-awaited Warhammer Online is slated for early 2008.

The U.S./European subscription gaming market grew significantly in size to \$875 million in 2006. That number is expected to increase to \$5.6 billion by 2011. France is expected to achieve significant growth over these next five years, followed closely by Spain and Italy, though Germany is predicted to remain the top market for online gaming subscriptions in Europe, and the U.S. will remain the West's largest market for online gaming.

Asian/Pacific: Led by companies such as Shanda, NetEase, CDC, Nexon, The9, and WebZen, the Asia/Pacific gaming market is projected to grow from \$5.9 billion in 2006 to \$7.5 billion in 2011.

Currently China and South Korea are the leading gaming markets for the Asia/Pacific region, but Japan is quickly gaining traction, and is expected to be the fastest growing segment of the Asia/Pacific market.

However, the online gaming market in the Asia/Pacific market is and likely will remain regionally segregated due to vast cultural and linguistic barriers. What is a success in one segment of this large market will not necessarily be a success in another segment. For example, in June 2007, Japan-based games company SEGA shut down its Chinese online games

division, citing a lack of familiarity with the Chinese online game market.

Indeed, despite the substantial head start of foreign games, Chinese domestically-produced games now account for 64.8 percent of the entire online gaming market in China. Part of the success has been credited to the General Administration of Press and Publication (GAPP), which has implemented policies to help spur domestic growth, but cultural factors cannot be underestimated.

Overall: Worldwide online game revenue is expected to increase from \$6.9 billion in 2006 to over \$13.1 billion by 2012.

What's popular?

Worldwide, online game players have a vast array of options when choosing a game. World of Warcraft (WoW) still continues to dominate the U.S./European market, with over 3.5 million reported subscribers (8.5 million worldwide), and currently accounts for 54 percent of the subscription market revenue. The following list shows the most popular subscription games for the NA/EU market:

1. World of Warcraft
2. Runescape
3. Final Fantasy Online
4. EVE Online
5. Star Wars Galaxies

These estimates are as of July 2007, and are drawn from public sources, where available. Lord of the Rings Online is excluded from these results as being too new for data to be available.

In 2006, subscriptions were still the leading revenue source for online games worldwide. But

in eastern markets, subscriptions are only moderately important in determining popularity of virtual worlds. Most measures of success are cited in peak concurrent usage (PCU) due to the long standing popularity of PC cafés (or baangs). World of Warcraft is popular in the Asia/Pacific market as well, proving to be a rare crossover hit. Top games for the Asia/Pacific market include:

1. Fantasy Westward Journey
2. Zengtu Online
3. World of Warcraft
4. Westward Journey Online 2
5. Yulgang Online

Trouble Spots

Following the outbreak of "gamer addiction clinics" in China, the government sought to curb addiction through legislation in 2007. Through the use of "fatigue" controls, the legislation mandates operators restrict duration of game use for minors by reducing the benefits to players who stay logged in for three to five hours, with no benefit over five hours of play. The legislation has met with subtle resistance from Internet cafes and game publishers. Nevertheless, the concern about game addiction is spreading. Parents in Korea have also become concerned that pre-paid game cards are contributing to addiction.

Games have also faced challenges from censorship in eastern markets. The9 (World of Warcraft operators in China) recently modified the appearance of the "Undead" race to appease censors and make things "less scary"—the "Undead" are part skeleton, part flesh. The revised models now show no skeleton, and show tombstones instead of corpses.

How Online Games Make Money: Predominant Business Models

Online gaming has been primarily subscription-driven for years, although “free to play” models are becoming standard in Asian/Pacific markets. While subscription still accounts for the majority of revenue in western markets, different approaches, such as free to play and pay to play with micropayments, are being explored by Western game companies. Western consumers have been slower to warm to micropayments, but with the help of the music industry and the popularity of services like iTunes, they are gaining traction. Micropayments are already popular in Asia/Pacific markets where, after the metered time model, subscriptions never really caught on. The following are predominant business models in the online gaming market, with a slant towards persistent world gaming.

Pay to Play Models

Subscriptions: At present the predominant business model for online games in the U.S./European market is the monthly subscription, providing 87 percent of the market revenue. This monthly fee covers the ongoing community support and development of new content through the life of the MMOG, as well as the massive bandwidth requirements. Generally, the current fee for a “first class” game is \$14.99 per month in Western markets, and has remained steady with a moderate inflow of titles. While subscriptions are important to the Western market, other international markets do not have the same dependence on them. The Korean MMOG “CABEL” (2005) is the only recent successful launch using a monthly subscription base.

Metered time (PC baangs/PC cafés): The original business models for online gaming were built on charging the consumer for gameplay on an a la carte basis, through connect-time fees or pay per play. One legacy of the connect-time model (charging per hour of service) continues to affect the field at present; games are built to maximize the amount of time people spend online. The most successful games continue to keep people online for many hours each month (anywhere from 40 to 80, in the case of some persistent worlds).

One of the standard business models for persistent worlds in Asia is tied to PC cafés, also known as “PC baangs” (rooms). An increase in broadband penetration has contributed to a decrease in baang usage and a slight uptick in personal subscriptions, and government regulation has helped encourage operators to explore new revenue models.

Free to Play Models

A new entrant to the Chinese gaming market, CDC Games, pioneered the “free to play” model in 2005 with MMOG Yulgang Online. Basic play was free while CDC offered “value-added services” instead of the traditional metered or subscription models for revenue.

The quick and profound success of CDCs (peak concurrent usages hovering around 300,000 strong) encouraged many other publishers to flock to the concept in droves. Major player Shanda Entertainment announced it would provide free gaming services for the online games it promoted during the year. After posting zero income for the end of 2005, Shanda proceeded to post profits equal to its best ever quarter on record in Q3 2006. On the heels of the market leader, companies such as Soft-world and Network Science Technology adopted similar models. Approximately 84 percent of online games in China’s gaming market launched in 2006 fall into the “free to play” category.

Retail product, free time: In this model, players purchase a retail product (client) and play for free online perpetually thereafter. The publishers of many session-based games and a handful of casual games find it worthwhile to offer free online play with the purchase of the client. For MMOGs, this is not a common model used throughout the life of a game, but it is industry standard to offer a month or two of free play with a retail purchase. Allowing players to invest some time in their character(s) free of charge, frequently causes an attachment to form to their characters, increasing their willingness to ante up for a subscription.

Pay for content: In 2005, NCsoft implemented a “pay for content” model for Guild Wars. Guild Wars followed retail sales of the initial game with periodic, optional “expansions” introducing new content, to replace subscription revenues. Guild Wars reports that in the US/EU, 3,555,000 accounts have been activated to date.

Virtual property: “Virtual property” is the term used to describe artifacts in persistent world games that people value, in real money. Persistent worlds like Fantasy Westward Journey and World of Warcraft are filled with things like magic weapons, armor, houses, in-game money, inventories, and characters built up over hundreds of hours of play.

People buy and sell these items on eBay or ItemBay, other Web sites, or through private means regardless of legal concerns, with thousands of dollars trading hands every day. The fastest growing segments of the online gaming market are virtual item sales and digital distribution. The topic of virtual property is further discussed in the section titled Real Money, Not-so-Real Items.

Advertising: In this model, everything is free to the consumer, with revenue coming from sponsorship, or quite often product placement. This model is commonly used for "Web based" and casual games offered through web portals.

Other Revenue Streams

In addition to the core business models described above, resourceful game operators have found other ways to generate revenue from the customer relationship. With so many games on the market worldwide, churn is an ever-growing problem, so more and more companies are latching on to strategies that tap additional sources of revenue from ardent players.

Expansion packages: Expansion packages are add-ons with new content and features, historically released for an online title at a rate of about one per year. Retail distribution being a more important channel for U.S./European releases, and broadband being more limited, expansion packs are predominantly a Western phenomenon. They generally retail for premium prices (\$39.95 and up).

Collector editions: Many MMOG companies increase up-front revenues through releasing collector's editions of their games. Collector's edition packages tend to include pins, collector's maps, and other knick-knacks, as well as in-game awards or special items.

Pre-order incentives: MMOG operators typically offer pre-order incentives—for example, special items within the game to lock-in all-important early sales.

Character transfer: With the rise of special servers, as well as the ongoing problem of server overcrowding, companies have started to offer character transfer services. Character transfers from one server to another range from

\$9.99 to \$50 for 1 character up to \$125–\$375 for a full set of characters, the upper end including item transfer. Many games in the Western market do this now, often placing restrictions on items or amount of game currency that can move with a character, and/or limiting the number of transfers within a particular timeframe.

Account transfer, character renaming: After noting a trend in account sales a few years ago, Ultima Online developed a fee-based "safe account transfer" service allowing players to transfer their account to another person, without risk of fraud. In conjunction with this service, they adopted the "character renaming" service, which, when combined with the above service, allows the new account holder to personalize an account by changing the names of the characters. Although many games offer this service at present, they do not typically allow the option to change the account name as these are often tied into billing systems. Companies that offer single character transfers to different accounts typically require the same person be the owner of both the origin and destination accounts.

Character leveling services: This service allows players to circumvent the often tedious task of building a character. By paying a small fee to the game operator, a player's character is instantly leveled up, quickly making them competitive, if not in player skill, at least in "stats." While efforts from operators to sell "advanced characters" represent one of the first steps forward to directly selling in-game property, only a handful of games (including Ultima Online and Guild Wars) offer this service currently. The growing secondary industry of virtual service providers has taken on this task, however, and quickly added it to their menu of "services."

Multi-game combination accounts: To keep players loyal to a company's primary game offerings, as well as entice players to try out additional offerings, some companies offer multi-game combination accounts. Sony Online Entertainment (SOE) introduced a "Station Pass," allowing customers to access seven games operated by SOE for \$29.99. Combination accounts are not common yet, although several companies who operate several MMOGs (such as NCsoft) are making movements toward this type of offering.

Premium service/Servers and special events: Although selling "virtual experience" has proven popular (paying money for additional in game events), concentrating that experience into a single server though additional service in game and a "special server" was first demonstrated to be successful in text-based Simutronics games.

EverQuest followed suit, becoming the first graphic role-playing game to do so. Generally, for a premium server to be successful it must offer at least the following features: limited population, personalized/expedient customer service, access to private/new areas and content not available to standard subscribers, and the ability to play on regular servers if desired. This is not a common business model.

Real Money, Not-so-Real Items: Virtual Property & Services

The virtual property economy has gained attention in recent years from those outside the games industry, proving much larger than most believed. Most virtual property trading started with individual players earning and selling their

prizes as a side, then full-time, business. Following these entrepreneurs, an increasing number of firms have been set up expressly for the purpose of virtual trading and services such as character leveling. The market size of real-money trade of virtual items has been estimated to be worth \$1.82–\$2.09 billion in 2007.

The market for virtual property and services, including direct sales of digital assets, premium in-game experiences, and processing of player to player transactions is expected to keep increasing for persistent worlds along with digital distribution, matching subscription revenue by 2012.

The player reaction to the presence of virtual property sales in persistent worlds is very mixed. These feelings range from outspoken loathing (common reasons including “it breaks immersion” and “it is not fair”), to acceptance and sympathy for users who are disadvantaged by the inability to spend as much time in-game as their counterparts but still wish to compete. There are even those who view the buying and selling of virtual property as an inevitable outgrowth of interacting in a virtual society.

The reaction of gaming companies is equally mixed in Western markets. Several companies have banned outside sales of virtual items from their game outright. Others, such as Electronic Arts directly support the task by offering virtual items for sale, and also offer other services to make transactions easier, including a “safe account transfer” service in Ultima Online. Sony Online adopted the “Station Exchange” as an answer to provide a secure environment for transactions for in-game coins, items, and characters. After one year, revenue for the company from the Station Exchange was \$274,083, although \$1.87 million passed through the system. An increasing number of games are joining the bandwagon, offering in-game items for real-world cash.

In Eastern markets, the business models of games are changing to “cut out the middle man,” with virtual world providers allowing everything to be purchased by microtransactions and leaving the basic “game” or world free to play in. There is little to no stigma towards Eastern consumers of virtual property.

All this exchange of virtual property and money has raised a question: Who, ultimately, is the owner of the virtual property? At the moment, the legal status remains unclear in all markets, although the debate is vigorous. The China Internet Network Information Center (CNNIC) issued a report in spring 2007 stating 61 percent of gamers have had virtual assets stolen, and 77 percent feel that the current online atmosphere is unsafe for virtual assets. NTS (Korea’s national tax service) started adding VAT automatically as part of financial transactions in July 2007, though it is unclear who exactly will end up paying these taxes since most terms of service define in-game items and currency as belonging to the developer. There are still many topics to work out in this area, including ownership of content and how far real-world laws can be applied within a virtual setting.

Persistent Worlds: Looking Ahead

Persistent worlds will continue to present an interesting opportunity in the realm of entertainment over the next few years. The current base of people that are part of one or more persistent worlds is expected to grow, spurred by the increased use of the Internet in daily life. This increased usage of the Internet, coupled with the increased availability of broadband, sets the stage for growth for all areas of the Internet, including persistent worlds.

Persistent Worlds—Not just for computers anymore!

While it is likely that persistent worlds will remain PC-based in the near future, console developers are already working on bringing this phenomenon to different platforms. Sony’s “Home” virtual world announced in July that it would support social net-working and have mobile phone tie-ins, encouraging users to stay connected wherever they go. The “Home” service is designed for the PS3 and allows users to have an avatar and an apartment that can be furnished with free or purchased content. Not taking into account the Nintendo Wii and Playstation 3, the number of households connected to the Internet via their console system grew to over 4.4 million for the U.S. market in 2006.

Moving Beyond Games

The influence of Western persistent worlds is also being felt keenly on the Asia/Pacific market, as countries aim toward developing their own “home grown” versions of popular offerings in the North American/European markets:

- An upcoming Chinese virtual world is being developed by MindArk and being billed as “a three-dimensional eBay.” Designed for high capacity and telecommuting, this June 2007 announcement led David Liu, Chief Executive of CRD, to establish the bold claim that virtual worlds would generate about 10,000 jobs in China.
- More 3-D synthetic worlds are taking off. HiPiHi is in beta testing mode, noted for a remarkable resemblance to Second Life, cites a “complex social structure and a full functioning economy.” HiPiHi isn’t the only entrant to this category, as Shanda has announced plans to develop a product, and UOneNet Technology’s “uWorld” also making waves.

Games and social chatting are not the only application for virtual worlds. The market has jumped into novel applications of the technology, with new ones being reported weekly.

- Japanese politician Kan Suzuki became one of the first of Japan's lawmakers to establish a cyber office in the virtual world Second Life. The plan has not gone as smoothly as he would hope, as Mr. Suzuki may find himself in violation of Japanese election law. According to the law, Web sites cannot be created or updated during the campaign period.
- In Vancouver, BC, Canadian police are also turning to Second Life to gain the attention of tech-savvy players—and hopefully gain a few real-life recruits in the process.
- Japanese companies such as Toyota and Honda have already firmly established themselves in virtual worlds, as have many graphic design and Web production companies.
- Major firms such as IBM and Sun have already developed corporate controlled virtual worlds designed for internal use only. These “intranet metaverses” are used to enhance communication between offices and promote collaboration.
- Companies have developed for the express purpose of serving as content creators in virtual worlds, and are hired out by companies wishing to establish a presence and promote their brand within certain virtual worlds.
- From an economic standpoint, each persistent world has the potential to become a microcosmic economy. This unique characteristic has enabled economists to observe and experiment with economies in a way that have never been possible before.

- Academics have been able to use persistent worlds to carry out noteworthy studies in sociology and psychology.
- Persistent worlds have become interesting for business for example, advertising and product placement within the worlds, as well as a whole market surrounding virtual property.

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