

August/September 2019

# VIDEO GAMING / E-GAMING LAW UPDATE

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## Main Quest

### Is My Loot Box Legal?

Mitigating Legal Risk for Game Developers and Publishers

On April 5, 2019, the U.S. Federal Trade Commission (FTC) announced that it will be holding a public workshop on August 7, 2019, to examine consumer protection issues related to “loot boxes” — in-game rewards players can buy while playing a video game. The FTC’s decision to consider potential regulation of loot boxes is just the latest in a long line of legislative and administrative reactions to this growing trend in video games.<sup>1</sup> While, to date, most attempts to ban or regulate loot boxes have been unsuccessful, the growing scrutiny of such practices by government officials deserves the attention of anyone with a connection to the video game industry. In this article, we discuss potential challenges facing loot box systems, current attempts to regulate this mechanic and strategies for reducing risk during this period of uncertainty.

#### The Rise of the Loot Box

The term “loot box” generally refers to any mechanism allowing players to obtain a set of unknown virtual items for use in a game. A loot box could be a booster pack in a collectible card game, a weapons crate in a first-person shooter or a llama-shaped piñata in a battle royale game. In most, though not all, instances of loot boxes, the available items have varying degrees of rarity, with more desirable items appearing less frequently.

Loot boxes and other micro-transaction mechanics have grown increasingly popular in the last several years, paralleling the growth of the free-to-play market and rising development costs across the video game industry.

#### Are Loot Boxes Legal?

Today, most forms of loot boxes remain legal and unregulated worldwide.<sup>2</sup> However, proponents of loot box regulation argue that the chance and rarity mechanics make loot boxes akin to gambling and constitute predatory practices focused toward minors.<sup>3</sup>

While this comparison may seem overblown to some (particularly those with small children who are familiar with the rampant use of “surprise mechanics” in toys), a careful examination of relevant statutes and analogous cases demonstrates the potential risk posed by loot box systems. For example, the three federal statutes governing online gambling (the Wire Act, the Unlawful

<sup>1</sup> Press Release, FTC, [FTC to Hold August Workshop on Consumer Issues Related to Loot Boxes](#) (Apr. 5, 2019).

<sup>2</sup> See below for a discussion of the narrow exceptions to this general principle.

<sup>3</sup> See, e.g., [Letter from Sen. Margaret Wood Hassan, D-N.H., to Patricia Vance](#) (Feb. 14, 2018); [Senator Hawley to Introduce Legislation Banning Manipulative Video Game Features Aimed at Children](#), Josh Hawley (May 8, 2019).

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Internet Gambling Enforcement Act and the Illegal Gambling Business Act), as well as each state's individual gambling laws, generally require three elements for a particular activity to constitute an illegal "wager": (1) risking something of value, (2) on the occurrence of a chance event, (3) for a potential valuable prize.<sup>4</sup> Arguably, each of these elements may be satisfied by certain loot box systems.

For instance, courts have already held that in the context of mobile games, virtual currency constitutes something of value and thus may satisfy the first element.<sup>5</sup> Additionally, given that many loot box systems involve some aspect of chance, a court would likely find the second element satisfied as well.

With respect to the final element, while most courts that have considered the issue in the context of mobile games have found that "prizes" awarded in video games *do not* constitute a thing of value where players cannot sell such prizes,<sup>6</sup> the U.S. Court of Appeals for the Ninth Circuit recently held that in the context of a casino games mobile app, the chips that a player could win *were* an item of value, because the chips allowed the player to continue playing the game.<sup>7</sup> While this decision remains an outlier, it establishes at least one arguably analogous situation under which a video game system has been determined to constitute gambling.

## Potential Sources of Challenge

Given the above discussion, video game developers and distributors should keep in mind the potential avenues for challenges to loot box systems. For example, state attorneys general may bring criminal or civil actions against a company if they believe that a game's loot box system constitutes illegal gambling. Additionally, most states provide a private right of action to anyone who lost money as a result of an illegal gambling operation under either a *qui tam* statute or anti-gambling statute.<sup>8</sup> Thus, aggrieved consumers need not wait for government enforcement to challenge a loot box system.

<sup>4</sup> See, e.g., 18 U.S.C. §§ 1084, 1955; 31 U.S.C. § 5362; Cal. Penal Code § 330b (California law); 720 Ill. Comp. Stat. 5/28-1(a)(1) (Illinois law); Wash. Rev. Code § 9.46.0237 (Washington law).

<sup>5</sup> See, e.g., *Kater v. Churchill Downs Inc.*, 886 F.3d 784 (9th Cir. 2018); *Soto v. Sky Union, LLC*, 159 F. Supp. 3d 871 (N.D. Ill. 2016).

<sup>6</sup> See, e.g., *Mason v. Machine Zone, Inc.*, 851 F.3d 315 (4th Cir. 2017); *Phillips v. Double Down Interactive LLC*, 173 F. Supp. 3d 731 (N.D. Ill. 2016); *Sky Union*, 159 F. Supp. 3d 871.

<sup>7</sup> See *Kater*, 886 F.3d at 787. It should also be noted that in *Sky Union*, the court stated that a digital prize would constitute a thing of value under California's gambling statute if it extended the privilege of playing the game for free. See *Sky Union*, 159 F. Supp. 3d at 880.

<sup>8</sup> See, e.g., *Humphrey v. Viacom, Inc.*, No. 06-2768 (DMC), 2007 WL 1797648 (D.N.J. June 20, 2007).

Even if loot boxes are presumptively legal and do not constitute gambling, other challenges to the marketing and sale of loot boxes may be raised. For example, consumers may also bring lawsuits based on consumer protection or false advertising statutes to the extent that loot boxes are marketed in an arguably misleading way. Indeed, a putative class action lawsuit was recently filed against Epic Games alleging that loot boxes in *Fortnite* were falsely and unfairly advertised.<sup>9</sup> Moreover, sensitivities about the marketing of loot boxes and scrutiny of video game companies' practices may be heightened to the extent that loot boxes may be targeted to minors.

## Recent Attempts at Regulation

In light of these concerns, many government officials, both in the U.S. and abroad, have taken steps directed at regulating loot boxes. For example, state legislatures in at least four states have introduced bills aimed at regulating loot box sales.<sup>10</sup> While many of these bills have since died in committee, bills in Indiana, Minnesota and New York remain under consideration. Further, the Protecting Children From Abusive Games Act was introduced in the U.S. Senate this year, seeking to prohibit loot boxes and pay-to-win mechanics in *any* game targeted toward or played by minors.<sup>11</sup>

Internationally, the issue of loot boxes has been considered by at least a dozen countries, three of which — Belgium, the Netherlands and China — have outlawed loot boxes to some extent.<sup>12</sup> In fact, the gambling commissions of Belgium and the Netherlands found that most forms of loot boxes constituted gambling under the same wager, chance and valuable prize structure discussed above.

<sup>9</sup> See *R.A. v. Epic Games, Inc.*, No. 5:19-cv-00325 (E.D.N.C. filed Feb. 28, 2019).

<sup>10</sup> See, e.g., H.R. Con. Res. 224, 30th Leg. (Haw. 2019); H.R. Res. 199, 30th Leg. (Haw. 2019); H.R. HF 4460, 90th Leg. (Minn. 2018); S. 6266, 65th Leg., 2018 Reg. Sess. (Wash. 2018); Assemb. 2194, 2017-18 Reg. Sess. (Cal. 2018).

<sup>11</sup> *Senators Hawley, Markey, and Blumenthal File Legislation to Stop Manipulative Video Game Practices Aimed at Children*, Josh Hawley (May 23, 2019).

<sup>12</sup> See *Research Report on Loot Boxes*, Belgian Gaming Commission (Apr. 2018); Tracey Tang, *China: A Middle-Ground Approach: How China Regulates Loot Boxes and Gambling Features in Online Games*, Mondaq (May 16, 2018); *Loot Boxes and Netherlands Gaming Authority's Findings*, Dutch Games Association (Apr. 19, 2018).

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## Strategy Guide

**Given the uncertainties present in the current landscape, video game companies should examine their loot box practices closely and keep in mind the following strategies to minimize legal risk:**

Take steps to avoid creating a wager, chance or win/loss structure required for a finding of gambling. For example:

- Make the currency used to purchase loot boxes also acquirable from in-game action, not simply available for direct purchase.
- Remove chance by showing players in advance what they will get in a loot box (a strategy Fortnite has recently employed).
- Allow players to use duplicate items to progress in the game in some other way, so loot boxes always provide players with some value.

- Prevent players from exchanging items received in loot boxes, and enforce pre-existing prohibitions on sales of items and/or accounts.

Consider parental controls on loot box purchases made by minors;

Ensure that loot boxes are promoted with clear, conspicuous terms or fees that consumers could not plausibly contend are “hidden” or obscured; and

Continue working with lawmakers and regulators through self-regulatory bodies like the ESRB to foster an environment of self-regulation.

## Side Quests

### Recent judicial decisions and enacted statutes or regulations that are likely to impact the video game industry

***Steve Jackson Games, Inc. v. inXile Entm’t, Inc.*, No. 91225722 (T.T.A.B. 2019)**

- In a nonprecedential opinion, the TTAB sustained Steve Jackson Games, Inc.’s opposition to inXile Entertainment, Inc.’s application to register the mark AUTODUEL for video games, based on Steve Jackson Games’ use of its own AUTODUEL mark for a series of tabletop role-playing games.
- The TTAB found that tabletop games and video games, while distinct, may be related in the eyes of consumers, and it noted that trademarks for video games may be licensed to makers of tabletop games, and vice versa.
- The TTAB highlighted that Steve Jackson Games presented evidence that it had previously licensed the AUTODUEL mark to Origin Systems, Inc. for a vehicle combat video game and that a related mark, GURPS, had been used by Steve Jackson Games along with licenses from the makers of the Myth and Alpha Centauri video games.
- This holding, and a similar holding from *In re Restoration Games, LLC*, No. 87457730 (T.T.A.B. 2019), provide a good

reminder that when clearing a name for an upcoming game, developers and publishers should not only look to existing video games but other related media entertainment, such as tabletop or card games, to avoid claims of likelihood of confusion.

***Hayden v. 2K Games, Inc.*, No. 1:17CV2635, 2019 WL 1299943 (N.D. Ohio Mar. 21, 2019)**

- On March 21, 2019, the U.S. District Court for the Northern District of Ohio granted in part 2K Games, Inc.’s motion to dismiss claims brought against it by tattoo artist James Hayden in connection with 2K’s depiction of NBA players (along with their tattoos) in its NBA 2K series of video games.
- In December 2017, Hayden filed suit against 2K asserting claims for direct and indirect copyright infringement, unjust enrichment/restitution, violation of the Visual Artists Rights Act, and for a judgment declaring 2K’s copyright registrations in its NBA 2K16, 2K17 and 2K18 games invalid on the grounds of fraud on the Copyright Office.

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- The court dismissed Hayden's unjust enrichment claim, holding that it was preempted by the Copyright Act, and dismissed Hayden's declaratory judgment claim, holding that because 2K had never asserted its copyright registrations against Hayden, nor threatened to do so, there was no judicable case or controversy.
  - However, the court denied 2K's attempts to dismiss Hayden's copyright claims seeking statutory damages and attorneys' fees for tattoos that were not registered when NBA 2K16 was published but had been registered by the time NBA 2K17 and 2K18 were released.
    - 2K had argued that yearly installments of a video game franchise that feature the same depictions of the same players in each release do not constitute separate acts of infringement but rather should be considered a continuing series of acts.
    - The court rejected this argument, holding that further discovery was needed on this issue.
  - The court has set a settlement conference for November 7, 2019.
- Genuine Enabling Tech., LLC v. Nintendo Co., Ltd.*, 369 F. Supp. 3d 590 (D. Del. 2019)**
- On February 25, 2019, the U.S. District Court for the District of Delaware granted Nintendo of America, Inc.'s motion to transfer venue in a patent infringement action.
  - The patent venue statute, 28 U.S.C. § 1400(b), provides that "[a]ny civil action for patent infringement may be brought in the judicial district where the defendant resides, or where the defendant has committed acts of infringement and has a regular and established place of business," and constitutes "the exclusive provision controlling venue in patent infringement proceedings."
  - The U.S. Supreme Court recently clarified this statute in *TC Heartland LLC v. Kraft Foods Grp. Brands LLC*, 137 S. Ct. 1514, 1518 (2017), holding that, in a patent infringement action, venue is proper only:
    - In a district within the corporate defendant's state of incorporation; or
    - In a district where the corporate defendant has a regular and established place of business and has committed acts of infringement.
  - Nintendo of America is incorporated in Washington, and while it is registered to do business in Delaware, it does not have a regular and established place of business there.
- Accordingly, the court held that venue was improper in Delaware and transferred the case to the U.S. District Court for the Western District of Washington.
- Color Switch LLC v. Fortafy Games DMCC*, No. 118-cv-00419-DAD-JLT, 2019 WL 1427975 (E.D. Cal. Mar. 29, 2019)**
- The U.S. District Court for the Eastern District of California granted a motion to dismiss in a copyright infringement action based on a forum selection clause in the parties' publishing agreement.
  - In 2015, plaintiff Color Switch LLC developed a mobile game and entered into a publishing agreement with EyeBoxGames FZE (later Fortafy Games), based in the United Arab Emirates, to assist with publishing and marketing the game.
  - The agreement contained a forum selection clause stating that the agreement itself, as well as any noncontractual obligations arising out of or in connection to the agreement, will be governed by UAE law and submitted to the exclusive jurisdiction of the Court of Dubai.
  - After Color Switch terminated the publishing agreement, Fortafy refused to turn over the most recent version of the game, claiming that the agreement gave it the exclusive rights to any updates.
  - Color Switch filed suit, but Fortafy moved to dismiss, citing the forum selection clause, and notified the court of pending related matters in the UAE.
  - The court granted the motion, holding that the forum selection clause applied not only to Color Switch's breach of contract claims but to its copyright claims as well. It noted that the Ninth Circuit has not yet weighed in on the question of whether copyright claims are subject to forum selection clauses when the contract at issue is raised as a defense, but that the Ninth Circuit has held that such clauses cover tort claims if the interpretation of the contract is necessary to their adjudication.
  - The court also determined that enforcing the forum selection clause would not deprive Color Switch of its day in court, as the UAE had adequate — if less robust — copyright protections. Nor was enforcement contrary to public policy.
  - On April 23, 2019, Color Switch appealed the decision to the Ninth Circuit, and briefing is set to begin in September 2019.

## Patch Notes

### New litigation filings and proposed legislation and regulations that may lead to important legal developments in the video game industry

#### **AM General LLC v. Activision Blizzard, Inc.**, No. 1:17-cv-08644-GBD-JLC (S.D.N.Y. filed Nov. 11, 2017)

- On May 31, 2019, Activision Blizzard, Inc. the publisher of the popular Call of Duty series, filed a motion for summary judgment in a trademark infringement lawsuit brought against it by AM General, LLC, the manufacturer of Humvee vehicles for the U.S. military.
- AM General has accused Activision of trademark infringement, trade dress infringement, false advertising, false designation of origin and dilution in connection with Activision's use of Humvee vehicles in its Call of Duty game.
- Activision's brief argues that AM General cannot satisfy the U.S. Court of Appeals for the Second Circuit's *Rogers v. Grimaldi* test, which governs the use of trademarks in expressive or artistic works.
- Briefing is ongoing and the court has scheduled oral argument for September 17, 2019.

#### **Niantic, Inc. v. Global++**, No. 3:19-cv-03425-JST (N.D. Cal. filed June 14, 2019)

- The creator of the popular mobile game Pokémon Go and the recently released Harry Potter: Wizards Unite geo-location game, has sued alleged hackers for copyright infringement and is seeking a preliminary injunction.
- In the complaint, filed June 14, 2019, Niantic, Inc. claims that Global++ and several of its members acquired legitimate versions of Niantic's games and then worked around the security systems to create unauthorized derivative programs that allow other players to cheat.
- Niantic's complaint alleges copyright infringement for its code, in addition to claims sounding in violation of cybersecurity laws, unfair competition and breach of contract.
- Briefing on the preliminary injunction is ongoing and the court has scheduled oral argument for September 4, 2019.

#### **Iron Maiden Holdings Ltd. v. 3D Realms Entm't ApS**, No. 2:19-cv-04606-DSF-JC (C.D. Cal. filed May 28, 2019)

- On May 28, 2019, Iron Maiden Holdings Ltd., the holding company for heavy metal band Iron Maiden, filed a complaint against 3D Realms Entertainment ApS, most famous for its Duke Nukem franchise, alleging trademark infringement as a result of 3D Realms' latest game — Iron Maiden, a retro first-person shooter.
- While Iron Maiden is most recognized for its music, it has also released a number of video games, including a 2016 mobile game titled "Legacy of the Beast."
- The complaint alleges that Iron Maiden not only shares a similar "look and feel" with Legacy of the Beast but trades on several additional associations with Iron Maiden, including: the name of its main character, Shelly Harrison, which is similar to Iron Maiden founder Steve Harris, the game's use of a logo presented in a "steel-cut" font similar to Iron Maiden's logo and the title featuring a "bomb" emoji that is similar to Iron Maiden's "Eddie" mascot.
- The complaint includes claims for trademark infringement, false designation of origin, unfair competition and dilution.

#### **Tenney v. FaZe Clan Inc.**, No. 19STCV17341 (Cal. Super. Ct. filed May 20, 2019)

- Professional eSports gamer Turner Tenney — known as Tfue — has sued gaming company FaZe Clan, Inc., alleging that FaZe Clan has trapped him in a "grossly oppressive, onerous and one-sided" contract.
- The complaint includes claims for termination of Tfue's agreement with FaZe Clan, unfair business practices, return of money had and received, *quantum meruit*, breach of contract, breach of fiduciary duty and a declaration that the agreement contains anti-competitive restrictions on Tfue.
- In the complaint, Tfue alleges that FaZe Clan's practices are industry standard, and that eSport companies generally are preying on young and unsophisticated gamers to saddle them with unfair contracts, stripping them of most of their earnings and exploiting them for the companies' own profit.

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- In addition to the complaint, Tfue has filed a petition with the California Labor Commissioner's Office that seeks to have FaZe Clan forced to acquire a talent agency license, and Tfue has alleged that FaZe Clan uses its unlicensed status to avoid complying with certain labor regulations.

***Epic Games, Inc. v. C.B.*, No. 5:19-cv-00250-FL (E.D.N.C. filed June 18, 2019)**

- On June 18, 2019, Epic Games, Inc. filed a lawsuit against a teen user, accusing the user of using cheating software for its popular Fortnite game and alleging claims for direct and contributory copyright infringement, circumvention of technological measures in violation of the Digital Millennium Copyright Act and trafficking in circumvention devices.
- Epic alleges that the gamer, a minor, circumvented measures Epic placed into Fortnite to prevent players from cheating, and that he offers his cheating software to other players for a fee.
- Epic also alleges that the player operates a YouTube channel, where he has posted videos that show him cheating at the game, and which he uses to promote his hacks.
- This lawsuit represents the seventh time Epic has gone to court to stop accused cheaters

***Twitch Interactive, Inc. v. John and Jane Does 1 through 100*, No. 3:19-cv-03418-WHO (N.D. Cal. filed June 14, 2019)**

- On June 14, 2019, popular game streaming service Twitch, owned by Amazon.com, filed a lawsuit demanding that a group of currently unknown users cease using bots to stream inappropriate content, including violent videos, hardcore pornography, and copyrighted movies and television shows, on its Twitch.tv service.

- The complaint alleges that the users relied on bots, new accounts and accounts bought from other Twitch members to coordinate an attack on the Twitch service, flooding the directory dedicated to the game Artifact with the inappropriate content.

- In response to efforts by Twitch to combat the attack, the users also created a Twitter account and website that used the Twitch logo and trademarks.

- The complaint contains claims for trademark infringement, breach of contract, fraud and trespass to chattels, and Twitch is seeking a preliminary injunction as well as restitution, statutory, compensatory and punitive damages, and attorneys' fees.

**FTC to Hold Public Workshop on Loot Boxes**

- As mentioned in the "Main Quest" article above, the FTC will be holding a public workshop on August 7, 2019, to discuss consumer protection issues related to video games' use of loot boxes.

- The workshop will bring together members from the industry, consumer advocates, trade associations, academics and government officials to discuss concerns regarding the use and marketing of loot boxes, as well as consider whether loot boxes and similar in-game mechanics should be regulated.

- Topics will include the current in-game transaction landscape, research regarding consumer behavior (and particularly children's behavior) as it pertains to in-game transactions, and consumer awareness and education about in-game transactions.

- The FTC is currently accepting public comments and will continue to do so following the workshop, through October 11, 2019.

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