

RSAConference2018

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SESSION ID: LAW-RO2

GAMIFICATION: EMERGING REGULATION (AKA “MAKE MONEY AND AVOID JAIL”)

Behnam Dayanim

Chair, Advertising & Gaming Practice
Global Co-Chair, Privacy & Cybersecurity Practice
Paul Hastings LLP
@bdayanim

Why Do We Play Games?



- Competition
- Unpredictability
- Possibility of winning a “prize”
- Because they are fun
- To pass the time



- Games are seeping into financial services, HR, healthcare

Social Games Industry - Evolution



- In 2007, the social games phenomenon was introduced to the world through Facebook.
- In 2013, there were over 750 million people worldwide playing social games.
- In 2017, 2.2 billion (IBISWorld).



Gamification!



skillz



Agenda



- What are they? (With some numbers)
- Some (more) numbers
- What are they not (we hope)?
 - Introduction to Gambling Law
- Issues to consider
 - Social casino/sweepstakes
 - Skill games
 - Brief note on DFS and e-sports
- Impact of new technologies in managing risk and compliance
 - Geolocation
 - Cryptocurrencies
 - Data analytics
- Okay, what about the “avoiding jail” part of this talk? How do I do that?

Social Games Are a Big Deal



- \$108.9 billion in revenues in 2017, across all platforms and categories (NewZoo)
- Smartphone and tablet account for \$46.1 billion and are growing at 19% year over year
- Fantasy sports \$7B in 2017, 11% annual growth despite legal difficulties
- Nearly three-quarters of players of social games (excluding fantasy sports and skill games) are women (SuperData Research); over 90 percent of players never pay
- Top 10 market entrants in social account for over 80% of market (Statista); DFS is even more concentrated

Where can you find gamers?



Everywhere...

	Country	Ms	\$M
1.	CHINA	802	\$27,547
2.	USA	261	\$25,060
3.	JAPAN	120	\$12,546
4.	GERMANY	73	\$4,378
5.	UK	62	\$4,218
6.	SOUTH KOREA	47	\$4,188
7.	FRANCE	57	\$2,967
8.	CANADA	33	\$1,947
9.	SPAIN	38	\$1,913
10.	ITALY	43	\$1,875
11.	RUSSIA	113	\$1,485
12.	MEXICO	84	\$1,428
13.	BRAZIL	140	\$1,334
14.	AUSTRALIA	22	\$1,234
15.	TAIWAN	21	\$1,029
16.	INDONESIA	72	\$880
17.	INDIA	429	\$818
18.	TURKEY	49	\$774
19.	SAUDI ARABIA	25	\$651
20.	THAILAND	32	\$597

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GAMBLING LAW

The World Is Not Monochromatic



- Gambling laws vary widely from country to country
- Some countries construe the term more broadly than others
- I am a US lawyer!!
- Focus on US, with observations on others as appropriate – and with all requisite disclaimers.



Federal Laws



- “Unlawful internet gambling” means a “bet or wager [that] is unlawful **under any applicable Federal or State law** in the State or Tribal lands **in which the bet or wager is initiated, received, or otherwise made.**”
 - UIGEA; 31 U.S.C. § 5362(10)(A).
 - The intermediate routing of electronic data are not considered in that determination.
- Wire Act prohibits using a wire communication facility (such as the telephone or internet) to transmit “bets or wagers on any sporting event or contest.” 18 U.S.C. § 1084.
- PASPA – sports
- Other statutes rely on underlying violation of Wire Act or state laws.

State Laws



- ▶ Gambling generally requires 3 elements:
 - ▶ **Consideration:** The payment of something is required to play the game
 - ▶ **Chance:** The outcome of the game is influenced by chance
 - ▶ **Prize:** Money, money's worth or something of real-world/tangible value is awarded based on game play
- ▶ Evaluation of these games requires assessment of those elements, which is not always simple or straightforward



Sweepstakes



- What about those bottlecap promotions?
- Meet the Free Alternative Method Of Entry
- Some limits, state by state, notably:
 - “Clearly occasional and ancillary to the primary business of that person”
 - Questions surrounding use of mail-in AMOE



Regulatory Overlay



- “Reg GG” (required by UIGEA)
- Applies to financial transaction providers, although platforms and others have adopted similar models
- If quasi-gambling, will need to provide a **reasoned legal opinion** that it is **not** gambling and may need to geo-locate users
- Payment processing and platform access are gating issues for success; hence, this has become a de facto requirement for gaming operators

Why Do I Care?



- Game may be rejected by app store or platform
- Payment processing may not be available
- Class-action lawsuits
- State AG cease-and-desist and similar actions
- Jail!



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SOCIAL CASINO AND SWEEPSTAKES

The Basics of Social Games



- Common characteristics of social games:
 - Played for entertainment;
 - Game play is typically (not always) very simple;
 - Played through social networks; and
 - Players may play at little to no cost.
- Many games are designed with **social interaction** and **competition** among players in mind.
- Popular games include Farmville, The Sims, and Words with Friends.

Social Games – Business Models



Generally, there are **two business models** employed in the social games industry:

- Up-front cost for the game or application
 - Buy the application like Angry Birds
 - Not at issue here
- Free game or application with in-game purchases available to enhance the entertainment experience or linked to another paid product or service
 - Dominant model

Social Casino-Style Games



- All involve chance and rely on “sweepstakes” model
- Major Point of Difference:
 - Cash or merchandise awarded?
 - Promote the game or some other product or service (e.g., a savings account or health measure?)



Internet Sweepstakes Cafés



- Internet sweepstakes cafés allow patrons to purchase internet time, or sometimes prepaid telephone minutes or other office services. Patrons receive sweepstakes entries along with their purchase.
- Many cafés allow patrons to play simulated gambling games as a way of revealing whether they have any winning sweepstakes entries.
- Estimated as recently as 2015 that internet sweepstakes cafés earned over \$10 billion annually.

Sweepstakes Café Litigation



- Example: *State v. Vento*, 286 P.3d 627 (N.M., 2012)
 - Majority of customers paid to play the games, the vast majority of the internet time sold went unused (99.75%)
 - Patrons used sweepstakes winnings to purchase additional internet time, even though they still had time remaining in their accounts.
 - Finding: Lottery
- Example: *Lucky Bob's Internet Café, LLC v. California Dep't of Justice*, 2013 WL 1849270 (S.D. Cal. May 1, 2013)
 - 100 entries to the Sweepstakes for every \$1 of purchased internet time
 - Prizes ranging from 10 cents to \$3,000
 - 94% prize payout rate
 - Total of \$1,225,055 was spent for 204,176 hours of internet time, and 97.375% of the total purchased internet time was unused
 - Finding: Slot machine

Sweepstakes Café Laws



- Response: We need a law anyway!!



- Similar laws (albeit using different statutory formulations) have been passed in California, Colorado, Connecticut, Florida, Georgia, Kentucky, Louisiana, Massachusetts, Mississippi, New York, North Carolina, Ohio and Pennsylvania.
- Some laws clearly limit to placement in a business establishment (*e.g.*, Ohio); others do not

Sweepstakes Café Laws



- Some statutes are written so broadly – to avoid attempted circumvention – that they capture far more activities than internet sweepstakes cafés.
- Potentially capture even free-to-play games like social casinos, depending on their prize structure.
- In other words, they seem to eliminate the consideration requirement (similar to UK).
- Moreover, some states find that **mere additional play** may be viewed as a prize for gambling purposes.



- Florida
 - any machine or device or system or network of devices . . . that, **upon activation**, which may be achieved by, but is not limited to, the insertion of any . . . account number, code, or other . . . information, . . . is **directly or indirectly** caused to operate . . . if the user, **whether by application of skill or by reason of any element of chance or any other outcome unpredictable by the user**, may . . . receive any . . . thing of value.”
- Massachusetts
 - devices used to conduct sweepstakes through an entertaining display, where “sweepstakes” is defined to include games that award prizes based upon chance, “**with or without payment of any consideration**”; “Entertaining display” can include actual or simulated game play.

Recent social casino litigation



- In 2015, one plaintiffs' firm brought at least 6 lawsuits against various social casinos and other games, including:
 - Game of War (2), Big Fish Casino, DoubleDown Casino, Castle Clash and Slotomania.
 - A seventh suit since has been brought (by another firm).
- All games operated on a freemium model.
- Plaintiffs brought claims under state qui tam laws or unfair competition/deceptive trade practices
- All suits were decided in favor of defendants, until Ninth Circuit decision in *Kater*, which has created some uncertainty in market

Other Countries More Aggressive Or Less Developed



- UK and Belgium have asserted jurisdiction over social games
 - UK has found virtual game currency to have value
 - Belgium requires licensing if game allows spend in excess of strict limits
- Japan has imposed limits on “gacha”; industry has responded:
 - Estimates of cost to obtain certain items
 - Better controls to prevent illegal txns (e.g., sales disguised as gifts)
 - Banning gacha games that too closely resemble gambling (e.g., bingo)
- China restricts play time for minors (on all types of games) and requires disclosure of odds in the context of random loot boxes

Takeaways?



- Ever-increasing popularity
- Not a lot of US regulatory appetite to tackle any but the most abusive cases
- Some US legislative activity (Hawaii) and some legislative action elsewhere (e.g., China, Japan, Belgium)
- Private plaintiffs so far not had significant success
- *But* risk factors:
 - Not promoting a bona fide good or service
 - Awarding cash or merchandise
 - Not granting AMOE true equal status (chance of winning)
 - Not differentiating among the states where warranted
- Take care to note jurisdictional differences!

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SKILL GAMES

Skill Games



- Still comparatively small (revenue-wise) but growing



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- These games typically (although not always – see HQ) involve payment **and** prize
- Thus, key is “chance”; states have one of three standards
 - Predominance
 - Material Element
 - “Any chance”
- Evaluating quantum of chance is extremely challenging
- Predominance = 51%, but how measured?
- What is “material”? 10%? 20%? No clear answer
- And how measure – what metrics? See data analytics later!



- Many countries distinguish between games of skill and chance
 - E.g., Brazil, Germany, India
- However, some require licenses for skill games
 - Malta (home of large number of online gaming licensees); contrasts with Gibraltar (another large online licensing jurisdiction), which continues to focus on chance
 - France recently revised its regulations to include “games which functioning relies on the know-how of the player” (Article L.322-2-1, Security Code)
 - China prohibits games for profit, regardless of whether skill or chance

A Brief Word About Other Games



- Fantasy sports and e-sports
- Fantasy sports tend to rely on particular provisions of the UIGEA and on the premise that they are games of skill
 - They raise unique issues and are more and more becoming directly regulated under state laws
 - In Europe, they are generally regulated as a form of betting
- E-sports take on the character of the underlying game in contests between contestants (e.g., if the game is a game of skill, the contest is a skill contest)
 - Wagering on the outcome of others' contests is generally unlawful (unless structured like DFS)

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NEW TECHNOLOGIES?

Geolocation



- A staple of regulated gaming
- Robust, at sign-up and every session
- Less significant in non-gambling gaming context but still becoming more and more important





- Virtual currencies are not a legal “out”
 - Bitcoin= “something of value”
- FinCEN issued guidance in March 2013
 - Defined “virtual currency” as “a medium of exchange that operates like a currency in some environments but does not have legal tender status in any jurisdiction.”
 - “Convertible virtual currency” is virtual currency that has an equivalent value in real currency, or acts as a substitute for real currency.
- Many states have followed suit or are considering
- Bottom line: for our purposes, same rules apply as with fiat (in all countries)



- What you don't know can hurt you
- Track “unhealthy” or illicit play
 - DFS example – “insider” play
 - “Bet the mortgage” problems
- Skill gaming – support characterization of game
- Analytical rigor is required

Different types of analyses

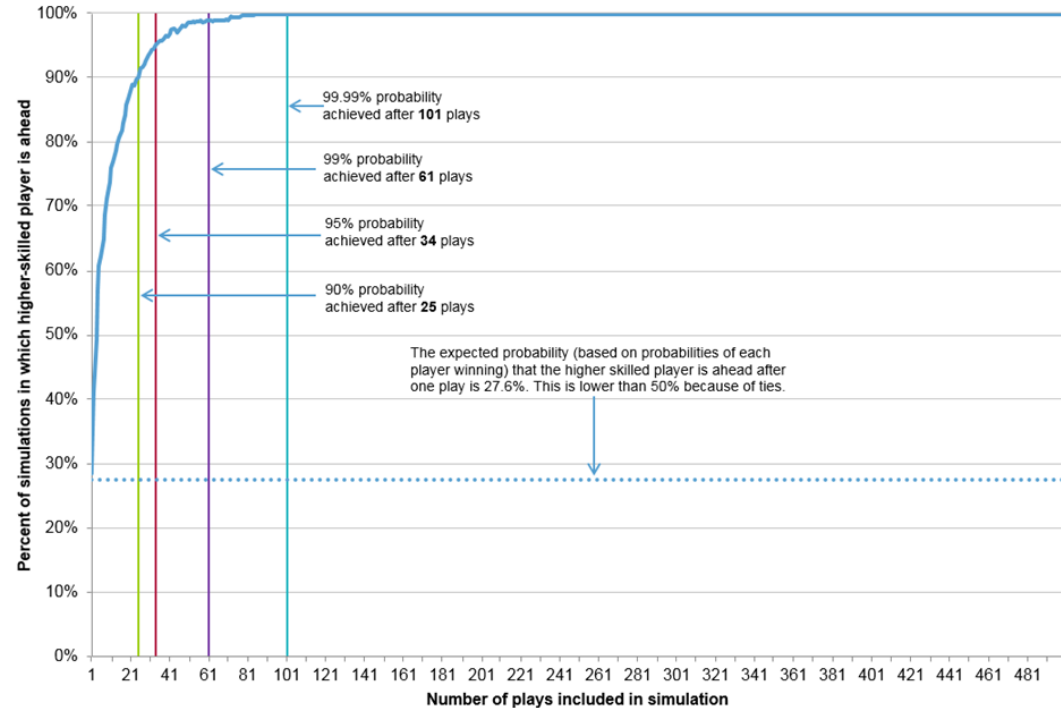


- There are different ways to measure skill
- Example 1: the “experience” test
 - Compare experienced players to novices and examine whether better game outcomes are associated with more play. If so, indicates a “learning curve” – i.e., that there is a skill to be mastered
- Example 2: the “correlation of win rate to skill” test
 - Compare win rates of “high-skill” and “low-skill” players. Possibly use AI as stand-in for players.
- Example 3: the “past success” test (accepted by *DiCristina* court)
 - Assess each player’s skill based on actual results, then group them into more and less skillful cohorts. Use **other** game results to determine the relative importance of the difference in skill between them.

“Experience” Test



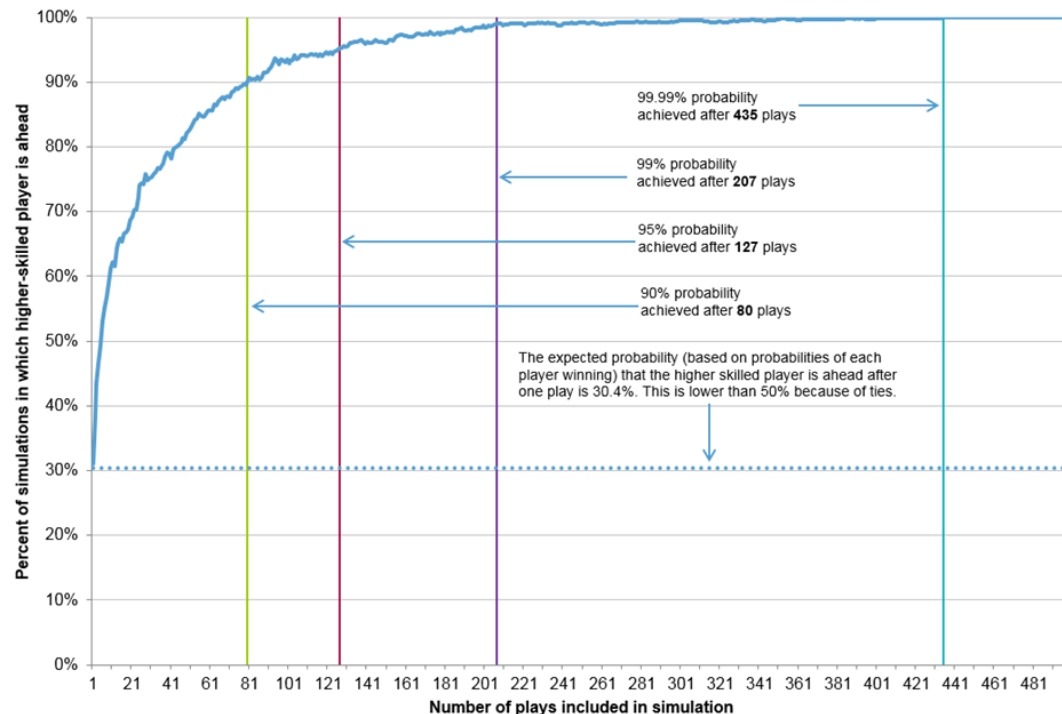
Number of plays required for a more experienced player to prevail over an inexperienced player



“Past Success” Test



Number of plays required for a player whose past success indicates greater skill to prevail over a player whose past success indicates lesser skill



Complicating Factors



- Length of play before skill advantage reveals itself
- How many players play enough to reach the relevant probability threshold?
- How demarcate low and high skill players for purposes of the “experience test”?
- What probability threshold suffices?
- How do varying pay-ins and pay-outs affect the data?

Staying Out of Jail (aka “The Apply Slide”)



- Understand the purpose and monetization model behind your game
- For casino-style games, ensure a robust AMOE
 - That may mean caps or similar approaches to numbers of entries/chances to win
- If you are a “pure” game model (not a non-game good or service), evaluate whether to offer cash/merchandise very carefully and be prepared to “justify” the game beyond the prize
- For skill games, understand the skill elements and be prepared to undertake a rigorous data analysis
- Formulaic legal recitations often will not suffice; neither will general focus on “federal laws” or “general state principles”
- **Be prepared to distinguish among states and countries**
- **Be prepared for a substantial legal and compliance investment**