Virtual Currencies (1):
Real Legal Issues

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“Points,” “coins,” “bucks” and other forms of virtual currency are becoming standard offerings for online game sites, social media sites, retailers and other businesses. Virtual currency systems generate revenue, provide low cost alternatives to credit cards for micropayments, offer prepaid solutions appealing to youth and other users without credit cards, and help companies build attractive loyalty programs. Although virtual currency systems are often used to sell digital content, they continue to become more complex – approximating real world currency as they allow purchase of physical goods and services from multiple merchants, offer cash redemption options, and facilitate peer-to-peer payments.

Even though the currency may be virtual, these systems pose real legal issues – both for issuers of the virtual currency and potentially for other network service providers and partners. Issuing virtual currency could subject an issuer to various state and federal regulatory regimes with wide ranging operational, financial and liability implications. These implications include restrictions on an issuer’s ability to expire the virtual currency or impose inactivity fees, requirements to give cash back for unused virtual currency, obligations to remit unused virtual currency balances to states, potential regulation as a financial institution, requirements to structure systems to avoid illegal lotteries, and privacy and data security issues.

This pair of articles highlights several key legal considerations and offers practical tips for companies that operate – or are considering developing – virtual currency systems.

The legal considerations and practical tips are illustrated in the context of an online game site run by the “Issuer” which implements a virtual currency system. U.S. revenues for virtual in-game goods alone are expected to grow approximately 50% from $1B in 2009 to $1.6B in 2010.<http://blog.jambool.com/>

Gift Certificate Laws: In order to increase revenue, the Issuer decides to sell virtual currency on a prepaid basis that can be used to purchase in-game virtual goods. Although virtual currency may seem different from paper gift certificates and plastic gift cards, virtual currency sold on a prepaid basis for later use or redemption by a user may be subject to state and federal gift certificate laws, including gift card provisions of the Credit Card Accountability Responsibility and Disclosure Act of 2009.<http://www.credit.com/credit_information/credit_law/understanding_the_credit_card_accountabi
Broadly speaking, state and federal gift certificate laws apply when consideration is paid for a record evidencing a promise to provide goods or services of a certain value to the bearer of the record. State and federal definitions vary, but can apply to virtual currency digital records and account balances. Gift certificate laws could restrict an Issuer’s ability to expire virtual currency, impose inactivity or service fees on virtual currency accounts, require conspicuous disclosure of key terms, and require an issuer to provide cash refunds of unused virtual currency. Certain exemptions apply, however, for gift certificates provided on a promotional basis without payment of money or other consideration from users.

**Practical Tips:** Build a virtual currency system taking into account applicable restrictions on expiration and fees, and establish consumer disclosures describing key terms.

If you will sell virtual currency and give it away for loyalty purposes, build into your system the ability to differentiate between virtual currency that can be expired and virtual currency subject to restrictions on expiration.

**Unclaimed Property Laws:** Several years after implementing a successful virtual currency system, the Issuer has a substantial amount of virtual currency that was purchased but never used or redeemed by users. Revenue from virtual currency that was purchased but never redeemed for virtual goods or other products and services is called breakage. State unclaimed property laws can apply to virtual currency breakage. If virtual currency breakage is deemed to be property under state unclaimed property laws, the Issuer could have an obligation to remit the value of unused or unclaimed virtual currency to one or more states after an applicable dormancy period (often 3-5 years). The state or states to which the Issuer might have to remit the breakage is determined according to established jurisdictional rules that take into account the location of the owner of the property (i.e., the user) and the state of incorporation of the company holding the breakage. Unclaimed property compliance in the virtual currency context is more complicated than programs involving paper gift certificates and plastic gift cards because virtual currency Issuers often maintain online user accounts with information about the identity and location of the user, whereas paper gift certificates and plastic gift certificates are often anonymous. Nevertheless, online systems with social networking features may, depending how they are structured, provide unique benefits unavailable in paper or plastic programs for providing full value of virtual currency to users or members of their social network – essentially minimizing the likelihood that users’ property will become abandoned or unclaimed.

**Practical Tip:** Scope the unclaimed property implications for your proposed virtual currency system early so there are no surprises several years later when dormancy periods have run. Involve relevant financial and tax advisers in the discussion.

More on the intersection of money in virtual worlds and law in the USA in the next column.

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