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Ninth Circuit Court of Appeals decision may put social gaming in doubt across several states

For several years, social gaming has been seen as a way to offer online gaming products to players in various United States jurisdictions that do not allow pay-to-play gaming. However, a new decision from the Ninth Circuit Court of Appeals has put the ability to offer such games in doubt in several states. The case, *Cheryl Kater v. Churchill Downs*, takes on the question of whether free-to-play online casino games with in-play purchases violate state gambling laws. While the Trial Court decisively concluded that such a system is permitted, the Appeals Court concluded the Big Fish free-to-play casino app (originally offered by Churchill Downs) was illegal gambling under Washington state law. Now, online gaming operators must decide what this case means for them in Washington state and elsewhere, as Jessica A. Feil, Associate at Ifrah Law, explains.

Background

Churchill Downs operated the Big Fish Casino app, a free-to-play app for online gaming. Players set up accounts on the app and were given free chips to play mobile slots, poker, and other popular casino games. If the players used all of their free chips, they had the choice to either wait a set period of time until their account was replenished with more free chips or they could purchase chips with real money. Importantly, players could never win a real world prize or cash out their virtual chips for real money.

Over the course of several years, Plaintiff Cheryl Kater purchased over \$1,000 worth of virtual chips to extend her gameplay. In her lawsuit, Kater alleged that the ability to purchase chips for additional gameplay rendered the Big Fish games illegal gambling under Washington state law. Specifically, she claimed that the virtual chips she purchased with real world money were a thing of value.

At the District Court, Churchill Downs prevailed on a motion to dismiss. Specifically, the lower court found that the virtual coins, even though they allowed the plaintiff to extend her gameplay, had no real world value, and thus the games did not constitute illegal gambling.

The Ninth Circuit finds real world value in virtual coins

The Plaintiff appealed her case to the Ninth Circuit Court of Appeals. There, a three-judge panel reversed the District Court ruling and concluded that the Big Fish games were illegal gambling.

The Court's decision turned on what constitutes a thing of value. Pointing to the very broad language of Washington's illegal gambling statute, the Court concluded that entertainment in the form of extended gameplay was a thing of value. Kater only won that because she paid real money to obtain additional virtual chips. The Court rejected Churchill Downs's argument that the virtual chips only enhance gameplay, not extend it, noting that the virtual chips are essential to continue play and thus were essential to the entertainment value. Upon finding that the extended gameplay facilitated by the virtual chips was a thing of value, the Court held that the games were illegal gambling under Washington state law.

Churchill Downs has petitioned for a rehearing before the full Ninth Circuit panel, but a rehearing and opinion could be months away. While awaiting the next steps, several operators have already blocked Washington state residents from playing their free-to-play

casino games. Further, several more cases have been brought in Washington state against gaming operators in light of this Ninth Circuit ruling.

Virtual currency in a real money world

This case is not the first time a federal court has considered whether the use of virtual currency in an otherwise free-to-play game implicates illegal gambling statutes. For example, in *Mason v. Machine Zone*, a District Court in Maryland considered whether virtual currency and virtual prizes were a real world thing of value. In that case, plaintiffs claimed that the mobile app Game of War, a game of skill that contained a casino-type element, was illegal gambling. Specifically, they claimed that the ability to purchase chips with real world money to play in the casino, which in turn allowed them to win virtual prizes to use in the game, rendered the entire experience illegal gambling.

The District Court and the Fourth Circuit Court of Appeals disagreed, finding that the ability to purchase virtual currency with real world money to win virtual prizes does not transform a game into illegal gambling. Those courts saw a distinction between the real world things of value and 'mere' virtual currencies and prizes. Similarly, the Northern

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District of Illinois has concluded on two separate occasions that virtual currency is not a real world thing of value.

The Ninth Circuit took notice of these cases but dismissed their relevance. In a single paragraph, the Court concluded that those three cases were inapposite because of the uniquely broad language in the Washington statute of thing of value.

How far does the Ninth Circuit's decision reach?

The Ninth Circuit judges focused on the broad language of the Washington statute that provides that a 'thing of value' is 'any money or property, any token' that can be exchanged for 'entertainment or a privilege of playing at a game or scheme without charge.' Notably, the Court called the language of the statute 'particularly broad.' However, Washington state is not alone. Other states such as Hawaii, Maine, New York, and Nebraska have identical definitions of 'thing of value' on the books. Yet, as seen in the *Machine Zone* case in Maryland, other courts are taking a more modern approach to mobile gaming.

Does this mean that free-to-play or freemium games are now illegal in all states with identical or similar definitions? Not quite. The Ninth Circuit opinion turned on a prior case from a Washington state Court of Appeals. In that case, *Bullseye Distributing LLC v. State Gambling Commission*, a state-level appeals court had occasion to interpret the same definition of thing

of value. That state court took an expansive view, finding that extended gameplay, which customers obtained with real money, constituted a thing of value. The Ninth Circuit, deferring to that state court's interpretation of state law, concluded the same.

Moreover, while the Washington statute is very broad, many other states have much narrower language in force. Some states, by either statute or case law, explicitly do not include extended gameplay or entertainment as a thing of value. Thus, free-to-play and freemium games are still permitted in many states.

Next moves for gaming operators

At this point, gaming companies are in a tough spot. They could elect to leave Washington while the case remains pending and the law unsettled. Alternately, some operators may take their chances until a final resolution is reached. Until the parties decide their next step, the rest of the industry is left waiting.

In the meantime, there are some steps companies can take to avoid similar pitfalls. For one, while the Ninth Circuit did suggest that the ability to trade and sell virtual currency on unapproved third party sites was not central to the decision, the judges nonetheless pointed out that the Big Fish games had a mechanism that allowed players to trade and sell their accounts and virtual currency on a secondary market. Other companies should learn from this and ensure that their virtual currencies can only be used on their platforms. Further, operators should clarify that

virtual currency is not to be traded on a secondary market via terms of service and enforce these terms of service rigorously.

In those jurisdictions with the 'particularly broad' definitions of thing of value, companies may elect to simply not offer the freemium model of their games. While freemium games are popular, the risk may simply outweigh the reward. Companies can still offer their games, simply without the option to buy additional virtual coins.

Finally, companies could petition state gaming commissions and boards for a review of their products. While Churchill Downs asked the Court to consider general advisory statements from the Washington Gambling Commission, the Court declined because the Commission had yet to issue formal guidance on social games. But if a company were to secure a favourable judgment from a gaming commission, courts would be obligated to give that finding deference.

Conclusion

This case highlights the tensions between state gambling laws that are many decades old and new gaming technologies. The *Big Fish* decision has created a great deal of uncertainty for the previously assumed safe world of social gaming. Companies would do well to tread carefully in Washington state for now. However, given the demand for freemium games among consumers, it seems likely that solutions will be available for those gaming operators willing to work within the guidance from courts and regulators.