

The world is not enough: law for a virtual universe

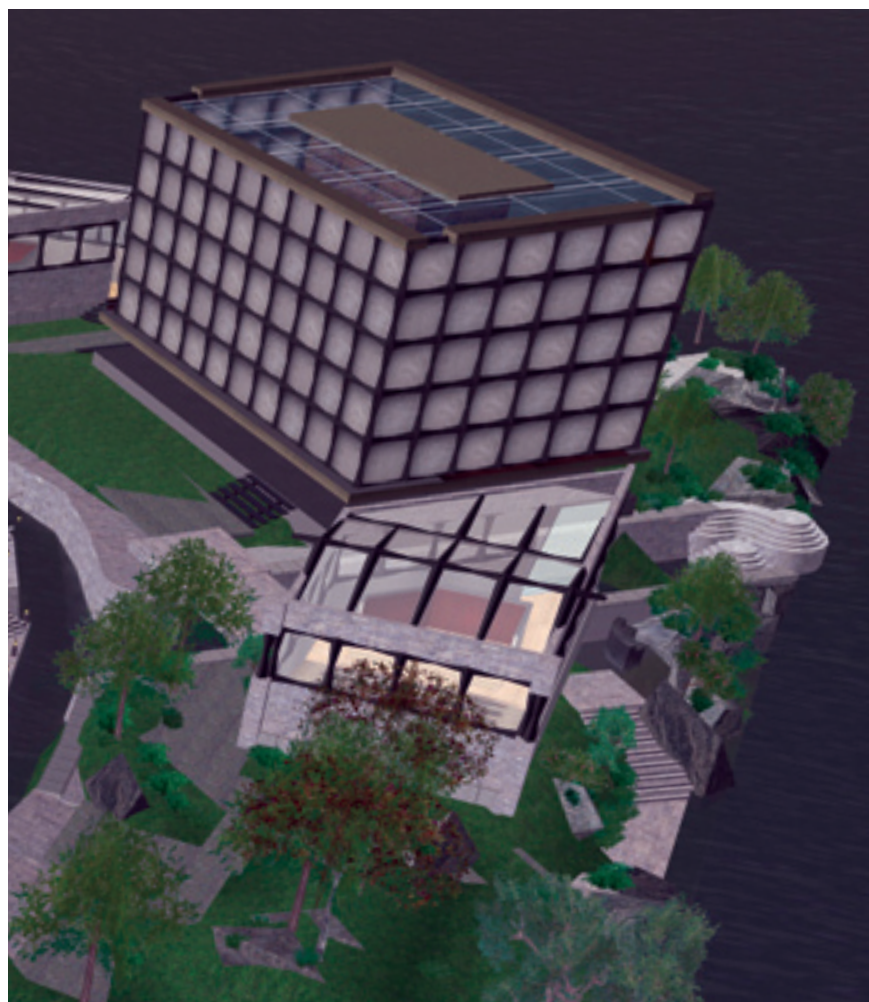
A dozen years ago many of Europe's law firms did not even have web sites. Now, very few do not depend on this technology: from using virtual data rooms, to allowing clients access to ongoing work via an intranet system, legal practices have grasped the value of computer-based tools.

Equally, clients have launched ambitious internet projects of their own and of course have been followed by streams of IT, IP and many other kinds of lawyers, eager to aid this burgeoning sector.

Today practitioners are gearing up for the next step in this legal adventure: virtual worlds – a new realm at the heart of the philosophy behind Web 2.0, the second wave of the web. Here, users create their own content and build online environments that others, including companies, take part in. And with this comes novel contractual challenges and legal risks for lawyers to master.

RICHARD TROMANS talks to experts in this fresh field of the law and examines what challenges lie ahead in Second Life, the most well-known of all virtual worlds

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Not all lawyers have heard of the virtual world of Second Life; indeed, even some of those who have believe it is just a video game. As one spokesman for a major US firm put it: "Sorry, but we don't think it's appropriate for partners to comment on a computer game." However Second Life is not a game, but an extension of the real world into cyberspace. And where reality extends so does the law. For David Naylor, a partner at UK firm Field Fisher Waterhouse, "The legal issues in Second Life are no less extant than legal issues in real life. In fact, they are more complex."

It is understandable that some lawyers do not appreciate the full impact of Second Life. After all, such 'metaverses' (see glossary on page 22) only exist on the internet. Equally, one does not deal directly with actual people but with the 'avatars' representing them. Using these avatars individuals run companies, own homes and interact with other avatars. Alan Sutin, a partner at the US's Greenberg Traurig, has a number of clients with business related to Second Life and other virtual worlds: "We take this area very seriously. It is small at the moment, but is growing rapidly and will be very important."

One might ask how a major firm like Greenberg Traurig profits from advising on

22 a virtual world, existing only on a computer screen. The answer is simple: real business deals occur in Second Life and real people make real money. Business ventures, even if they take place in the virtual world, still need legal advice. Dutch e-commerce partner Wolter Wefers Bettink, of Houthoff Buruma, comments: "We have been following Second Life for a year and believe there will be a flow of legal work when the value of commerce there increases. It may be like the internet in the early days, back in 1995: people at first thought it was just about communication and didn't see how it could be used for business." He predicts that as Second Life takes off, so will client demand for advice on how to operate there and litigate based on acts carried out in the metaverse.

For example, there are shops in Second Life where you can buy a pair of virtual Nike sports trainers for your avatar. That is to say, your avatar will wear these virtual shoes, just as you would if you bought real ones on the High Street. And they will cost you just a few real world dollars. However, there is a snag. Nike spokesman Charlie Brooks says: "Despite what some people think, Nike is not present in Second Life." Which means that those Nike shoes are not Nike shoes at all. Worse still, someone else is making money from them in the real world, even if the trainers sold are only virtual.

This is just the tip of the iceberg. While this could amount to trade mark infringement and passing off counterfeit goods, the perpetrator might claim nothing has 'really' happened as it was all virtual. Some Second Lifers are clearly acting as if external law does not enter their world. Others have gone as far as to set up their own legal jurisdiction: there is now a Second Life Bar Association, local court and even the Alonzo Law Firm, which appears to exist only in this virtual realm. However, practitioners say Second Life is not immune from external laws, and its users certainly cannot make up their own. Garrigues IT lawyer Sergio Morales notes that, although "digital territories have a lack of sovereignty, whenever an element

of connection exists with the legal system of a country, this legal system applies, regardless of the rules, policies or customs that are established [in the metaverse]."

This belief that what goes on in Second Life has no real-life legal implications has already gained a legal

term. Joshua Fairfield, an associate professor of law at Indiana University School of Law calls it the "magic circle", referring to "the metaphorical circle" that isolates in the mind of the user "the virtual world from outside influences, like law and the real world economy". But all lawyers

Virtual worlds glossary

Second Life: launched in 2003, it describes itself as "a 3D virtual world entirely built and owned by its residents". To date 6.8 million people have created avatars in Second Life. However, only around 400,000 log in each week. Owned and operated by California's Linden Labs, a privately held company.

Around \$1.5 million is spent by users in Second Life each day, with around \$200,000 being exchanged into Linden Dollars (the local currency) daily. Current exchange rate: \$1=L\$260.

Average price of land in Second Life is L\$10 per square meter. Average monthly total of land auctioned each month: 37 million square meters.

Companies present in Second Life include: IBM, Sun Microsystems, Philips, ABN Amro, Starwood Hotels and Reuters. Also, Field Fisher Waterhouse, the only European law firm to be based there.

Avatar: a representation in '3D' or 2D of an internet user. In Second Life and in other virtual worlds the user may change the appearance of the avatar considerably, buying them clothes, shoes and even hairstyles. Usually, these avatars operate under pseudonyms and do not use real legal names.

Metaverse: digital '3D' environments where humans interact with each other (socially and economically) in cyberspace. There are a number of different metaverses already. Second Life is focused on a more adult audience where creativity and social interaction are the main elements. For this reason it has gained the most interest from business. However, there are others of a similar nature, such as There, Moove, Active Worlds and Entropia. Also, a number of metaverses cater for gamers, such as World of Warcraft or Everquest. Although not seen as places for companies to set up businesses, these gaming metaverses, or 'massively multiplayer online role-playing games' (MMORPG), do generate large quantities of revenue and virtual goods.

Web 2.0: First coined in 2003, the term refers to the social and creative sphere of internet activity where users develop and display their own content and build social networks. Other than the growth of virtual worlds, this would cover the development of internet sites such as Facebook, YouTube and the use of 'wiki' sites to share knowledge.

IP rights: Linden Lab's terms of service agreement recognises residents' right to retain full intellectual property protection for the digital content they create in Second Life, including avatar characters, clothing, objects and designs. The company states: "This right is enforceable and applicable both in-world and offline, both for non-profit and commercial ventures. You create it, you own it – and it's yours to do with as you please."

Sources: Wikipedia and Linden Labs.



Richard Tromans' avatar relaxes in Second Life

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interviewed stressed this separation is a delusion: a trade mark never ceases to be a trade mark, even if it appears in an online dimension.

Given that actions in the virtual world have a real world effect, major companies like Nike cannot sit back and ignore it, and nor will their lawyers. As the Nike spokesman says: "It is a difficult situation, but big brands will have to get involved." Despite the risks of dealing with customers who believe they are in a no-law environment, companies are lining up to enter. IBM, Dell, Pontiac cars, ABN Amro, Philips and even UK law firm Field Fisher Waterhouse have all set up in Second Life, with dozens of others expected to follow. Some are there primarily to publicise themselves, while some promote their real goods as well as selling virtual products. Around half a million people log in each week to Second Life, interacting with each other and these companies. That is a lot of potential law suits, especially as the legal contracts governing all this business remain mostly untested.

Lawyers also need to appreciate that actual money is exchanged here. In Second Life one can convert real world currency into Linden Dollars (the pertaining currency), at a rate of approximately \$1=L\$260. Around \$1 million passes through this metaverse as Linden Dollars every day; which can then be converted back by its new recipients and spent in the real world – for the moment tax free, too. Yet there is no legal text book, nor law, in any country on how to handle Linden Dollars.

And this is only one of the many metaverses that exist. There are more than a dozen so far, each with its own currency, and they are growing fast. One US web company – IGE – is even offering to do currency exchanges between metaverses, estimating that by 2009 virtual assets existing only within metaverses will reach \$7 billion. However Second Life is expected to be the main target for law firms as it is where the big companies have gone and should provide the best opportunities to advise clients.

What are the legal issues?

As seen with the Nike example IP concerns are at the top of the agenda for lawyers looking at Second Life. Graham Smith, a partner with UK firm Bird & Bird, suggests a client could run into some tricky IP ground almost immediately: "IP rights are set out in the terms of service of Second Life and it's a contractual document like any other. A company will have a trade mark for real shoes; but will it have a registration for virtual shoes?" The answer is: probably not.

The terms of service provided by Linden Labs, the company that owns and runs Second Life, also allot IP rights to users that make their own content inside the world. However, Mr Smith points out that the metaverse users may have a contractual arrangement with Linden Labs, yet they do not have an agreement with each other. Potentially, you could have two avatars which have created something virtual arguing over their IP rights to something that does not exist in the real world – for example, a virtual shoe. According to Mr Naylor, even more bizarre IP situations could arise: "You may get someone whose avatar looks just like Brad Pitt and they could be sued for taking someone's likeness." If the person then makes their 'Brad Pitt' avatar behave very badly one could see a case for defamation of character.

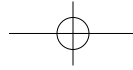
Then you have a number of legal issues connected to currency. For instance, how do you tax people in Second Life? According to Magnusson Law Firm IP expert Daniel Jastrun: "If it is real income then it is taxable, unless the government has dismissed income from virtual worlds from the tax base." US authorities, including Congress, have already looked at this issue and so far not come up with a clear answer. Meanwhile, in the UK, accountants KPMG have

recently urged the Treasury to start taxing income made inside Second Life. However, the general solution offered by most lawyers interviewed is that countries should not tax citizens until they cash their Linden Dollars into real world currency. On the other hand, there is nothing to stop someone keeping their Linden Dollars 'in world' forever. One could be a Linden Dollar millionaire and never pay a cent of tax unless you cashed in. Lawyers focusing on offshore tax could thus offer clients Second Life as a new jurisdiction in which to shelter their millions.

Equally, as Garrigues' Mr Morales notes, there is nothing to stop an avatar sending the virtual money to another avatar who in reality lives in a different location. So, real company profits could be turned into Linden Dollars and sent to an avatar friend, (who in real life lives in Bermuda), who could then cash them out for you tax free. Again, the law on virtual money transfers is non-existent.

This raises another concern: money laundering. Gide Loyrette Nouel IP and technology partner Grégoire Goussu confirms that it would be possible in Second Life to launder money. Avatars do not use people's real names and the personal data requested to enter the metaverse is quite minimal; with no more ID checking than is used to set up a Hotmail account, one could soon be funnelling thousands of dollars into Second Life and other metaverses. As Mr Goussu posits: "If Second Life is dealing with all this currency, is it acting as a bank? And if it is acting as a bank then it has obligations on reporting money laundering."

Gambling is also a difficulty in relation to such online environments. In the US gambling is illegal apart from in designated places such as Las Vegas and already directors of online gambling companies used by American citizens have been arrested when visiting the US. Second Life has a number of localities where it appears one can gamble Linden Dollars, although many are not listed as casinos. Linden Labs is a US company, but is gambling in a virtual world using



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only virtual currency really gambling? Harvard University professor Viktor Mayer-Schonberger says: "I understand that Linden Labs asked the FBI about this and all the FBI could say was, 'Good question'." Mr Mayer Schonberg suggests that as US citizens can "go abroad" to gamble, then perhaps one can also go to a virtual land to gamble.

On the same theme, capital markets lawyers should note that Second Life has a stock market with virtual companies that are freely traded within the metaverse. It too functions without any real world regulation, but again physical people are making actual money from it. No lawyers are checking the prospectuses or performing due diligence before advising a client to invest. There are no buy-out rules that would stand up in a real court either. The companies listed there may only be worth around \$50,000 at the moment, but these are early days for virtual worlds.

Finally, there are matters of a more visceral criminality. Top of the list is pornography and sexual crimes. Although it is highly distasteful, the following example shows just how messy legal concerns become in Second Life. There have been recent instances of avatars appearing as children that are having sex with other adult avatars. While the phrase 'child abuse' springs to mind, lawyers say such activity is not necessarily criminal in this context. Mr Mayer Schoenberg explains: "The legal issue here is consent and the need to protect minors. However, avatars only look like people. It is just a programme." Equally, the people behind the avatars are all adults as Second Life has age requirements. "I see no violation," he sums up.

There are also reputations at stake. As Bird & Bird German IP expert Fabian Niemann points out: "If you are a company that has set up your own island, what happens if this kind of thing happens on it?" Indeed, how can companies that arrive in Second Life control any behaviour on or near their property, from lewd acts to vandalism? Dr Niemann notes they cannot do much: "There is no police force in Second Life."

One could only allow vetted avatars to land on your island, but of course that would keep away the general public – which the company wanted to attract to their island in the first place.

Hypothetically, Linden Labs could be forced to pre-vet each piece of content before it is allowed in Second Life. However, as Second Life is as much about action as objects, that would mean vetting behaviour too. It would also require inspecting thousands of changes to the world every day. Houthoff's Mr Bettink confirms: "It would be a massive effort to pre-screen all content. If this was mandatory then any virtual world controller would face substantial liability issues." In fact, such a move would probably kill off virtual worlds.

Instead, Linden Labs and other metaverse controllers currently review content after it has been added and reserve the right to remove it. There is a terms of service agreement for Second Life users and Linden Labs can ban people from the virtual world who breach these conditions. However, in some cases that might not be good enough for a client who is upset with another Second Life participant. Yet for a company to sue an avatar over a complaint – for example, breaching IP rights – presents a totally different set of difficulties.

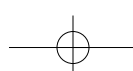
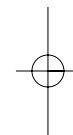
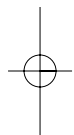
Litigation problems

All lawyers we spoke to agreed that as soon as a client decides to launch legal proceedings based on actions that have taken place in a virtual world, everything becomes complicated. "What jurisdiction are you going to hold the case in? Which law will govern it?" they asked. Linden Labs is based in California. The plaintiff company could be in London and the user being sued in South Korea. However, Linden Labs states that all disputes must be settled by arbitration in California, come what may.

Nörr Stiefenhofer Lutz partner Ulrich Michel says if the wrangle is between a company with a base in Second Life and Linden Labs, then this demand to hear the case in California would be fair: "This could be acceptable if the agreement between the company and Linden Labs is valid." However, if the dispute is between two 'non-professional' users, he points out: "Under German law regarding standard terms and conditions you would probably be in a position to contend that this is not valid." He notes you cannot force a consumer to travel to the US to dispute the delivery of a service that was taking place in Germany. Under UK law, meanwhile, Mr Naylor explains that "if a British company sells defective goods (via Second Life) to people in the UK, then UK law would apply". For instance, if Rolls Royce sold virtual cars to avatars and these cars ceased to function because the computer coding was faulty, a user could sue the company in the UK. Although, what an English judge would think of a row about a virtual car remains another matter.

But Jason Archinaco, a partner at US firm White and Williams, relates that a similar case has been heard in China already and the consumer won: a user of another metaverse called Redmoon lost \$1,210 worth of virtual products when his account was hacked and his goods stolen. He sued the metaverse company, to which "it countered that the virtual items had no value as they were just piles of data," says Mr Archinaco. However, the Chinese court awarded the case to the claimant and made Redmoon restore the lost items. 'Piles of data' can in fact be valuable it would seem.

Mr Archinaco has made legal history by becoming one of the few people to sue Linden Labs on behalf of a client in an infamous law suit known as *Bragg v Linden*. He is representing an American citizen whose virtual land was allegedly seized by Linden Labs after a spat broke out over land auctions in Second Life. The total value of the land may only be around \$5,000 but this lawyer is



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determined to win the case, albeit Linden Labs has brought in heavyweight US firm Reed Smith to help defend. Incidentally, Mr Archinaco has also faced problems with the demand to handle the proceedings in California, something the plaintiff does not want to do.

In fact, Linden Labs may have to brace itself for more legal action coming its way in years to come. IP expert Gianluca Gilardi of Italy's Studio Legale Sutti says that if an avatar was breaching a company trade mark in Second Life then rather than going after the person, a client might choose to target the servers ie Linden Labs: "We would sue where the server, the hardware is." This kind of tactic has already been used against web enterprises which have hosted content that businesses or individuals have disputed.

Although this approach appears quite straightforward, if the company then wanted also to sue the real person behind the avatar, things could become tricky. People in Second Life do not utilise their real identities. To commence a law suit against a user you need at least the name of the individual behind the offending avatar. And it gets more complicated. Daniel Westman, an academic at Stockholm Law Faculty, says: "The obligation to provide ID is different in each jurisdiction, yet Linden Labs may only answer to a US court to hand over the real ID of an avatar. In fact, it may not be possible for a person to start a civil case concerning Second Life because they will not be able to identify the other party." He explains that at least as far as Swedish law is concerned: "One has the right to access to justice if there has been a crime, but no one has a general right to know who someone is."

"We need procedural laws to handle disputes in Second Life," stresses Mr Westman, "or people could start to leave virtual worlds." With no such laws currently governing these activities, clearly any law firm hoping to create a

'virtual world practice group' should think very carefully about what that would entail: this is uncharted territory.

How law firms can use Second Life

But there are some lawyers who believe that beyond being a new field of law, virtual worlds could be useful for the profession in other ways. Top of the list is establishing a presence there. At this stage Field Fisher Waterhouse is the only firm in Europe to set up an office in Second Life, while in the US just a handful of mainly very small local practices have done so. Yet, this may be the shape of things to come.

Field Fisher's virtual office is two stories high, with a meeting room on the ground floor where there are displays and information about the firm. Upstairs there is more meeting space and an art gallery of pictures that also exist in real life. Sometimes the office is staffed by an avatar who in real life is a Field Fisher lawyer, but not continuously. Although the firm admits it could not yet do legal work via Second Life because it is not secure enough, Mr Naylor believes it is useful to be there: "It's a very good way to bring people together, for example, for presentations. It can also be used for recruitment." He adds that recently he, in the shape of his avatar, gave a tour of the office to someone who is now possibly going to join the firm's public relations team.

Many lawyers might wonder if such activities as holding a seminar will be effective in Second Life, but Harvard Law School has already started teaching some of its classes in the virtual world. Students turn up at the correct time and place and a professor shaped as an

avatar leads a class in real time and what appears as 3D. One could arguably achieve this over the internet using email, or a chatroom with multiple users. But seeing the law school teacher may improve the quality of learning, even if their avatar is a giant rabbit.

The big question for law firm marketers though is whether a practice could attract real clients by having a base in Second Life. Nörr's Dr Michel suggests: "Why not? We advertise in newspapers, we have a web site and we promote our services." Yet other firms are not so sure. Bird & Bird's Dr Niemann comments: "We have discussed it, but just being there is not enough. We would look to add value and we don't see a company like BMW seeking their lawyers via Second Life." He suggests that small practices which are seeking to attract the more High Street market of general consumers might be able to find clients. However he also stresses: "If you have an office and it is deserted, that to me is bad PR."

It is fair to say that even though the Field Fisher virtual office is very well made and nicely organised, on a number of occasions *the European Lawyer* has visited it there has been no one there. But then, lawyers cannot be expected to hang around in cyberspace all day hoping that a passing avatar is in fact the general counsel of a FTSE 100 company.

Practitioners do, however, say that if a more secure metaverse was created where one could guarantee avatars were of a serious business background, that might change things. Perhaps, just as the internet used to be a stronghold for geeks and technophiles, and has now turned into a place for big business, maybe virtual worlds will too. Who would bet against this latest development of the internet becoming as globally accepted in the future as having a web site is today? And if it is set to be the next big thing then any lawyer would be naive to assume they will not be impacted in some way. ■