

October 21, 2014

**VIA EXPRESS MAIL and E-MAIL**  
**CONFIDENTIAL TREATMENT REQUESTED**

Dana V. Syracuse  
Office of the General Counsel  
New York State Department of Financial Services  
One State Street  
New York, New York 10004  
dana.syracuse@dfs.ny.gov

**Re: Proposed Regulation of the Conduct of Virtual Currency Businesses,  
I.D. No. DFS-29-14-00015-P**

Dear Ms. Syracuse:

Attached please find our comments to the proposed Virtual Currency Regulatory Framework on behalf of the Entertainment Software Association. Thank you in advance for your consideration of our comments.

Please feel free to contact me with any questions.

Sincerely,



Arthur Middlemiss

October 21, 2014

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**Re: Proposed Regulation of the Conduct of Virtual Currency Businesses,  
I.D. No. DFS-29-14-00015-P**

Dear Ms. Syracuse:

We represent the **Entertainment Software Association** (“ESA”), the U.S. association exclusively dedicated to serving the business and public affairs needs of companies publishing interactive games for video game consoles, handheld devices, personal computers, and the Internet. The ESA appreciates the opportunity to comment on the New York State Department of Financial Services’ (“DFS”) Proposed Regulation of the Conduct of Virtual Currency Businesses (the “Proposed Regulation”). We commend DFS’s helpful definition of “Virtual Currency,” which correctly excludes from potential regulation digital units “that are used solely within online gaming platforms with no market or application outside of those gaming platforms” (the “Gaming Platform Clause”). We think this approach yields the right result given the closed nature of these systems, in contrast to other digital units that can be used as a medium of exchange in the broader economy. We write both to support this exclusion and to seek clarification regarding the Proposed Regulation’s application to certain products and services offered by ESA’s members.<sup>1</sup>

The ESA’s member companies publish video games and operate video game platforms. Some allow players to use digital units, or “points,”<sup>2</sup> to purchase and exchange various in-game enhancements, such as additional game levels and virtual skills or clothes for avatars.

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<sup>1</sup> On February 28, 2014, the ESA submitted a request that the Financial Crimes Enforcement Network (“FinCEN”) issue an administrative ruling pursuant to 31 C.F.R. § 1010.710, *et seq.*, to clarify that certain game play features within video games and integrated services operated by our members do not require our members to register as money services businesses (“MSBs”) pursuant to 31 C.F.R. §1022.380 and establish written anti-money laundering programs pursuant to 31 C.F.R. §1022.210. In large part, the ESA asked FinCEN to adopt the definition of Virtual Currency articulated by DFS in the Proposed Regulation. To date, the ESA has not received a response from FinCEN.

<sup>2</sup> As used here, and discussed further below, the generic term “points” refers to the multitude of means used to track a gamer’s accrued in-game and platform-level value. Depending on the game, these “digital units,” or “points,” may be called, *e.g.*, “gold,” “credits,” “jewels,” “diamonds,” or “coins.”

Additionally, some game platforms operate as “closed universes” in which gamers can use “points” to purchase in-game content and enhancements across multiple games available on that platform, or to enjoy other digital content available on the platform. Some ESA members also offer “points-for-prizes” systems that allow gamers to exchange “points” for a limited range of member-selected goods and services for use outside the gaming platform, *e.g.*, a t-shirt or coffee mug. In all of these scenarios, “points” are used solely for limited, member-defined purposes, and cannot be converted into Fiat Currency.

The Gaming Platform Clause specifically recognizes and plainly excludes “points,” *i.e.*, the digital units used in the closed universe scenarios, from the Virtual Currency definition. The Proposed Regulation also specifically recognizes and excludes customer affinity and awards programs. Given that the “points-for-prizes” systems operated by ESA members contain elements of these two excluded programs, we submit that the Proposed Regulation also excludes from its definition of Virtual Currency “points” used in a “points-for-prizes” system, and seek to confirm our reading of the Proposed Regulation.

In the alternative, we seek confirmation that “points” as used in a “points-for-prizes” system are excluded from the Proposed Regulation’s definition of Virtual Currency by virtue of the clause covering “digital units that are used exclusively as part of a customer affinity or rewards program, and can be applied solely as payment for purchases with the issuer and/or other designated merchants” (the “Customer Affinity Clause”). If, as drafted, neither the Gaming Platform Clause nor the Customer Affinity Clause is intended to exclude the type of digital units used in a “points-for-prizes” system, we ask that DFS consider an amendment to the Virtual Currency definition.

Finally, we seek confirmation that “digital units,” as that term is used in the Gaming Platform Clause and Customer Affinity Clause, reasonably include stored value codes. A stored value code is a multiple number/letter sequence known by the user that is used to identify the user to the service provider, *e.g.*, the code embossed on a gift card that enables the user to access value and purchase items from a service provider. Within our industry, a stored value code also can be auto-generated at the point of sale and represents the functional equivalent of a prepaid card, although the consumer does not receive a physical card. Stored value codes function as a proxy for “digital units” and merit similar treatment.

#### **A. Definition of gaming systems**

As background to our request, we provide more in-depth definitions of certain industry terms. In this letter, we refer to three different video gaming systems: Closed Universe (Single Publisher), Closed Universe (Multiple Publishers), and “Points for Prizes.” Each is described in greater detail below. With respect to all three systems, it is significant to bear in mind that “points” do not circulate for general purposes, cannot be converted into cash (or gift cards), and cannot otherwise be used as a cash replacement.

- **Closed Universe (Single Game):** Games use Fiat Currency,<sup>3</sup> including prepaid access, to buy and/or earn through game play “points” within a particular game, and the “points” have no value outside the game. Once accrued, gamers use “points” to enhance their in-game experience by redeeming them for virtual items<sup>4</sup> to be utilized within the game such as expansion packs,<sup>5</sup> additional game levels, and premium membership privileges.<sup>6</sup> In some cases, gamers may transfer the points to other gamers in the course of game play, but “points” cannot be converted into Fiat Currency or other real-world value.
- **Closed Universe (Multiple Games):** Gamers use Fiat Currency, including prepaid access, to buy and/or earn through game play “points” for exclusive use on the member’s game platform, a single virtual location or online network that offers games and other entertainment content offered by third parties and, in some cases, the platform operator itself. “Points” can be redeemed across the platform, but not beyond it. This simplifies how gamers obtain first- and third-party games and entertainment content offered on a network.<sup>7</sup> Gamers use “points” to enhance their game experience (*e.g.*, joining an online tournament, obtaining new games, upgrading virtual items for use within those games, downloading expansion packs, accessing additional game levels, and unlocking premium membership privileges) and to obtain other entertainment content, such as downloadable songs and movie rentals.<sup>8</sup> Likewise, some publishers allow “points” accrued in one publisher-created game to be used across multiple game titles and entertainment applications offered by that same publisher, *i.e.*, “points” acquired in Game A can be used in Game B, where both Games A and B are created by the same publisher.<sup>9</sup> “Points” cannot be used other than for limited member-defined, on-platform purposes, and cannot be converted into Fiat Currency or other real-world value.

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<sup>3</sup> As defined in the Proposed Regulation, Fiat Currency means government-issued currency that is designated as legal tender in its country of issuance through government decree, regulation, or law. Proposed 23 NYCRR §200.2(d).

<sup>4</sup> These virtual items, along with any “points” used to purchase them, are subject to the publisher’s End User License Agreement (“EULA”) and/or Terms of Service (“TOS”). Typically, these EULAs and TOS state that any virtual items and points associated with the account are licensed, not owned, may only be used within the game or service and, upon termination of the account, are not refundable except as may be required under applicable law.

<sup>5</sup> An “expansion pack” is software that provides additional game content, *e.g.*, extending a game’s storyline.

<sup>6</sup> Examples of premium or “velvet-rope” membership might include providing a gamer access to additional content or greater inventory capacity to store accumulated virtual items, and enabling a gamer’s avatar to advance beyond an otherwise set “skill cap,” *i.e.*, to provide the avatar different or enhanced abilities within the game.

<sup>7</sup> Some console networks use U.S. dollars and thus fall outside the scope of the Proposed Regulation. Notably, these systems do not allow gamers to transfer U.S. dollars from one gamer to the other and, in fact, do not allow the gamer to withdraw U.S. dollars from the game platform.

<sup>8</sup> Within individual games, but not at the platform level, gamers may be able to transfer “points” to other gamers.

<sup>9</sup> Another variant would include platform-wide “points” that can be used within specific games available on that platform. These points can be used, among other things, to acquire downloadable content, obtain premium membership privileges, and buy a limited range of virtual items. Separately, each game may have its own in-game currency that players use to buy other things, like equipment for their avatar. Again, whether accrued at the platform-level or within particular games, the value of the “points” cannot be converted back into Fiat Currency.

- **Points-for-Prizes systems:** Gamers use Fiat Currency, including prepaid access, to buy and/or earn through game play “points,” which may be used to purchase a limited range of member-selected goods and services for use outside the game or platform. For example, a publisher’s online marketplace may permit a gamer to redeem “points” for a collectible figurine, coffee mug, or t-shirt featuring an image of a favorite character, similar to how a video arcade may permit its patrons to redeem extra tokens for an ice cream at the snack bar. Gift cards or cash equivalents are not offered as prizes. “Points” cannot be used other than for member-defined purposes, and cannot be converted into Fiat Currency or, except as defined by the member, real-world value. Points-for-Prizes systems can exist within both Closed Universe (Single Game) and Closed Universe (Multiple Games) systems.

## **B. Analysis and Request for Clarification**

### **1. “Points” distinguished from e-currencies and e-currency brokers**

At the outset, the ESA commends DFS for including the Gaming Platform Clause in the Proposed Regulation, thus confirming that digital units, *i.e.*, “points,” used “solely within online gaming platforms with no market or application outside of those gaming platforms” are excluded from the definition of “Virtual Currency.”<sup>10</sup> The Gaming Platform Clause recognizes that the use of “points” in Closed Universe (Single Game) and Closed Universe (Multiple Games) systems does not constitute money transmission under New York law, and does not present money laundering or any other risk that would somehow undermine the banking system. We respectfully submit that the same is true with respect to the use of “points” in a “points-for-prizes” system.

Plainly, the Proposed Regulation was geared to address convertible virtual currencies such as Bitcoin, Liberty Reserve and E-Gold, which are wholly distinguishable from the activities of our members. Unlike Bitcoin or E-Gold, game publishers do not sell financial products. They do not seek to, and nor do they in fact, expand access to financial systems for their customers or anyone else. Their games are not designed to, and nor do they, facilitate the efficient transfer of monetary value from one person or location to another. Our members are not seeking to bank the unbanked. Nor do they seek to provide, or somehow unintentionally provide, a stable and secure method to move money anonymously around the world (as, for example, Liberty Reserve or E-Gold).

Our members are entertainment service providers. Gamers spend real world money for our goods and services for the same reason that they used to feed arcade tokens into Pac-Man or Skee-ball machines: to enjoy a game experience and perhaps, in a “Points-for-Prizes” system, win a prize. But unlike Bitcoin and E-Gold, “points” are not transferrable from one person to another for general purposes, *i.e.*, to buy real world things in the real world economy. To the extent “points” have nominal value in the real world, in a “Points-for-Prizes” system, the game publisher defines

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<sup>10</sup> Proposed 23 NYCRR §200.2(m).

and regulates it, in the same manner as the digital units described in the Proposed Regulation's Customer Affinity Clause. These simple facts demonstrate that "points" are not designed to be, and in fact are not, an alternative to Fiat Currency.

Given that "points" cannot be integrated or converted in any real sense back into the real world economy for general purposes, their money laundering utility is practically nil.<sup>11</sup> Furthermore, in light of the closed nature of these systems, they do not implicate the need for the various safeguards outlined in the Proposed Regulation, such as minimum capital requirements, financial disclosures, and detailed receipts for tax purposes, which may be better suited for currencies that act as a substitute for Fiat Currency.

Aside from transferability and convertibility, in terms of money laundering risk, "points" could not be more different from the services provided by unregulated money services businesses like Liberty Reserve (or its earlier incarnation, the New York-based E-Gold exchanger GoldAge).<sup>12</sup> Per its indictment, Liberty Reserve helped anonymous individuals move enormous sums of money across borders outside of the regulated financial system, and thus without fear of detection, for criminal purposes. Unlike Liberty Reserve, our members do not advertise to, or otherwise provide, "instant, real-time currency for international commerce, which can be used to send and receive payments from anyone, anywhere on the globe."<sup>13</sup> Indeed, "points" cannot be used by anyone to send and receive payments anywhere outside of the game or platform. Thus, from a money launderer's point of view, "points" are virtually worthless.<sup>14</sup>

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<sup>11</sup> In this discussion of the potential "convertibility" of "points," we acknowledge the phenomenon of unauthorized "real money trading" ("RMT") of "points" (and virtual game items purchased with those points or real currency) on certain third-party websites. RMT is the unauthorized practice of selling virtual items, e.g., a sword or a developed avatar, to another player in exchange for real money, i.e., Fiat Currency. Likewise, we acknowledge "gold farming," the unsanctioned RMT practice by which hired workers play MMO games to accumulate "points" and develop experienced players for sale to gamers. Conceivably, an entity engaged in RMT to facilitate anonymous real world money exchanges might require licensing pursuant to New York Banking Law § 650, and otherwise be subject to the federal Bank Secrecy Act. However, in general, our members do not participate in or otherwise control, sanction or profit from this unauthorized third-party RMT. Rather, our members' Terms of Service and EULAs prohibit it, and they take significant measures to eliminate it. As such, these practices should not be relevant to DFS's analysis. In any event, we submit that any attempt to launder criminal proceeds via unauthorized RMT would be wildly inefficient and ineffective. Nor is unauthorized RMT by third-parties a problem that imposing an anti-money laundering compliance program requirement on ESA's members would solve. For purposes of determining whether our members are subject to the Proposed Regulation, the mere fact that unauthorized third-party RMT exists in no way alters the sound conclusion that our members are not money transmitters because their games use "points" as defined herein.

<sup>12</sup> In 2006, the New York County District Attorney's Office brought a criminal indictment and a forfeiture action against GoldAge alleging, among other things, that GoldAge illegally transmitted money without a license in violation of New York Banking Law §650. See e.g., [http://decisions.courts.state.ny.us/fcas/FCAS\\_docs/2006SEP/30040297020061SCIV.PDF](http://decisions.courts.state.ny.us/fcas/FCAS_docs/2006SEP/30040297020061SCIV.PDF).

<sup>13</sup> *United States v. Liberty Reserve, et al.*, Case No. 1:13-CR-00368, Indictment, ECF. No. 18 ¶1 (S.D.N.Y. May 28, 2013).

<sup>14</sup> Indeed, in a "Points-for-Prizes" system, "points" represent the equivalent of arcade game-generated paper tickets that players use to claim prizes from behind the arcade counter. If the idea that a launderer would use criminal

**2. Analysis of the Gaming Platform and Customer Affinity Clauses**

For the reasons noted above, it seems readily apparent that DFS did not intend to include “points” as used in a “points-for-prizes” system within the scope of the Proposed Regulation, and that such a scenario is intended to be excluded by the Gaming Platform Clause, the Customer Affinity Clause, or both. The Gaming Platform Clause applies to digital units used “solely within online gaming platforms;” the Customer Affinity Clause applies to digital units used “exclusively as part of a customer affinity program.”<sup>15</sup> Read together, the two clauses would seem to exclude digital units generated within an online gaming platform that are then used as part of a customer affinity program, *i.e.*, a “points-for-prizes” system.

**3. Request for clarification that the Clauses should be read in tandem**

We urge DFS to clarify that the Gaming Platform and Customer Affinity Clauses should be read to cover the “points-for-prizes” game scenarios identified herein, whether under one or both of the clauses. Reading the Clauses in tandem would make clear that digital units (“points”) generated on an online gaming platform that “can be applied solely as payment for purchases with the issuer and/or other designated merchants, but cannot be converted into, or redeemed for, Fiat Currency,” are not within the scope of the Proposed Regulation. Thus, if a gamer generates “points,” *i.e.*, digital units, by playing the game, and then uses the “points” to purchase items from designated merchants (but can never “cash out” or otherwise turn the “points” into real-world value or Fiat Currency), then that circumstance should be covered by either one or a combination of the exclusions.

**a. Alternative proposal to amend the Clauses**

If DFS concludes that the Gaming Platform and Customer Affinity Clauses, as drafted, cannot be read in tandem to include digital units that are part of a “points-for-prizes” system, then we request that DFS amend section 200.2(m) of the Proposed Regulation as follows:

Virtual Currency shall not be construed to include digital units that are used solely within online gaming platforms with no market or application outside of those gaming platforms, nor shall Virtual Currency be construed to include digital units, that are used exclusively as part of a customer affinity or rewards program, **or that are operated within online gaming platforms for use in a rewards program,** and can be applied solely as payment for purchases with the issuer and/or other

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proceeds to play massive amounts of Skee-ball, obtain tickets, claim counter prizes and then sell the prizes for “clean” Fiat Currency seems absurd, so too should it be clear that “points” in a “Points-for-Prizes” system present low money laundering risk.

<sup>15</sup> Proposed 23 NYCRR §200.2(m).

designated merchants, but cannot be converted into, or redeemed for, Fiat Currency.

**4. Application of the Clauses to stored value codes**

As noted above, the Gaming Platform Clause excludes from the Proposed Regulation digital units “that are used solely within online gaming platforms with no market or application outside of those gaming platforms.” The term “digital unit” is undefined in the Proposed Regulation. We seek clarification that stored value codes used to purchase “points” constitute “digital units” to the extent that they are used solely within online gaming platforms (or as part of “points-for-prizes” systems) and cannot otherwise be converted into Fiat Currency. Thus, game-related stored value codes should be covered by the Gaming Platform Clause. This result makes sense because the stored value codes are acting as a proxy for a defined amount of game virtual digital units, *i.e.*, “points.”

**C. Conclusion**

For the foregoing reasons, we ask that DFS confirm that digital units, *i.e.*, “points,” used in a “points-for-prizes” as defined herein, which cannot be integrated back into the real world economy for general purposes or otherwise redeemed for Fiat Currency, are not covered by the Proposed Regulation. We believe that DFS’s confirmation that this is the case is sufficient but, in the alternative, we have proposed an amendment to the Proposed Regulation. Further, we ask DFS to clarify that “digital units,” as that term is used in the Gaming Platform Clause and Customer Affinity Clause, include stored value codes used to purchase virtual currency for use in online gaming platforms.

We are happy to answer any questions and address any concerns you may have, and look forward to speaking with you further about this matter, to which our members attach particular significance.

Sincerely,



Arthur D. Middlemiss  
(For the Entertainment Software Association)  
Lewis Baach pllc Kaufmann Middlemiss