

Inside the Game: Unlocking the Consumer Issues Surrounding Loot Boxes – An FTC Workshop
August 7, 2019
Segment 1
Transcript

MARY JOHNSON: Good morning, everyone. My name is Mary Johnson. I'm an attorney in the division of Advertising Practices in FTC's Bureau of Consumer Protection. Thank you for your interest in today's topic, "Consumer Issues Related to Video Game Loot Boxes and Microtransactions." Before we get started with the program, I need to review some administrative details. I don't have a catchy video to hold your attention, so please listen carefully.

Please silence any mobile phones and other electronic devices. If you must use them during the workshop, please be respectful of the speakers and your fellow audience members. Please be aware that if you leave the Constitution Center building for any reason during the workshop, you will have to go back through security screening again when you return. So bear this in mind and plan ahead, especially if you are participating on a panel, so we can do our best to remain on schedule.

If you received a lanyard with a plastic FTC event security badge, please return your badge to security when you leave for the day. We do reuse those for multiple events. So now some important emergency procedures. If an emergency occurs that requires evacuation of the building, an alarm will sound. Everyone should leave the building in an orderly manner through the main 7th Street exit. After leaving the building, turn left and proceed down 7th Street to E Street to the FTC emergency assembly area.

Please remain in the assembly area until instructed to return to the building. If an emergency occurs that requires you to leave this conference center but remain in the building, please follow the instructions provided over the building PA system. And if you notice any suspicious activity, please alert building security.

Now a little bit about photos and recordings. Please be advised, this event may be photographed and it is being webcast and recorded. So by participating in this event, you're agreeing that your image and anything you say or submit may be posted indefinitely at FTC.gov or on one of the commission's publicly available social media sites. Please also note that the microphones in this room on the stage are live. They will remain live throughout the day, even during breaks.

We certainly hope that you will have questions for panellists during the day. So please feel free to submit written questions for the panellists during the Q&A segments of each panel. Question cards are available in the hallway on the information table immediately outside the conference room. Also, FTC volunteers will be walking around the room with question cards. So if you need a blank card or you have a written question to submit, just raise your hand and an FTC volunteer will assist.

You may also submit questions for panellists via Twitter to @FTC using the hashtag #LootBoxFTC. Food drink and other necessities-- lunch is available here in the building from

11:30 to 2:00 PM. And between 2:00 and 3:00, there's some limited hours and services. After 3:00, it will be closed. The restrooms are located in the hallway just outside this conference room.

Finally, thank you to everyone who helped put together this event. That includes the staff of the Bureau of Consumer Protections division of Advertising Practices, division of Financial Practices, division of Litigation Technology and Analysis, and division of Consumer and Business Education. It also includes staff of the Bureau of Economics and FTC's event planning team, Office of Public Affairs, media team, and security management team.

And now I am pleased to introduce our bureau director to give opening remarks for today's workshop. Andrew Smith is director of the FTC's Bureau of Consumer Protection. He came to the FTC from the law firm of Covington & Burling, where he co-chaired the financial services practice group. Earlier in his career, Mr. Smith was a staff attorney at the FTC, where he focused on consumer financial protection issues and led the agency's efforts to make several rules under the Fair Credit Reporting Act.

Please join me in welcoming BPP Director Andrew Smith to the podium.

[APPLAUSE]

ANDREW SMITH: Thank you, Mary. So good morning, everybody. It's my pleasure to welcome you to our workshop, "Inside the Game, Unlocking the Consumer Issues Surrounding Loot Boxes." I probably should give our standard disclaimer that I speak only for myself and not for the commission or any individual commissioner. But thank you for being here at the Constitution Center or for joining us through the FTC's live webcast. And also, thanks to those of you following on Twitter.

We also thank the individuals and organizations who have taken the time to submit public comments or make suggestions for today's workshop panels. The comment period will be open until October 11 and we encourage you to submit written comments on issues discussed in the workshop. You'll find details on how to submit comments on our loot box workshop event web page.

So everyone-- children and adults-- plays video games. There's a video game out there for almost any interest, from action and adventure to sports and strategy. The video game landscape has changed dramatically over the last several years. Games today offer rich graphics, sophisticated storylines, and can be accessed through mobile devices, computers, and console systems. By one estimate, more than half of game players play on more than one platform, with mobile being the most common.

The popularity of gaming is such that it has become something not just something that people do but an activity that people watch, discuss, debate. Players live stream their video game play, YouTubers and others broadcast shows about gaming, and eSports competitions attract hundreds of millions of viewers worldwide and have prizes in the millions of dollars. But let's get to the issue that brings us here today, the purchase of loot boxes and other in-game items.

The ability to make in-game purchases isn't new. It's a feature available over multiple platforms. These purchase options, often referred to as microtransactions, encompass a range of digital items, such as cosmetic skins to outfit an avatar, in-game currency, bundles, upgrades, bonus levels, and containers with random assortments of mystery rewards called loot boxes, loot crates, or loot chests. Alternatively, players may earn virtual items or in-game currency by investing time rather than money, such as hours of gameplay, competing in time challenges within the game, or racking up bonuses for logging into the game daily.

While the rewards may be virtual, microtransactions are a very real revenue stream for game developers and publishers. Game companies report billions of dollars in revenue from such transactions. When it comes to loot boxes and other randomized digital rewards, these so-called surprise mechanics-- surprise, here I am-- are not always welcome surprises. There have been anecdotal reports of consumer spending hundreds to thousands of dollars in pursuit of coveted items.

Many people have expressed serious concern about whether these mechanics are predatory or contribute to gambling-like behavior, particularly as to children or with people who already struggle with gambling or addictive problems. In addition, do consumers, especially children or adolescents, adequately understand what they're purchasing and how much time or money they're spending? Are the disclosures adequate? For example, disclosures about the odds of obtaining specific loot box items, especially if those odds may change depending on game behavior.

The FTC has a long history of looking at consumer issues involving the video game marketplace. We've issued several reports on marketing violent entertainment to children, we've published guidance for parents about video games and kids, and we've carefully examined cases in which there is a potential for consumer injury. Video game microtransactions raise important consumer issues and ones that we look forward to discussing today. So here's today's lineup.

This morning, we're going to explore the in-game microtransaction landscape, who plays video games, the history of loot boxes and game monetization more generally. What is a loot box? And what are the different types of in-game purchases? How do players make these purchases? What's the role of in-game microtransactions in video games and other considerations from a developer's perspective, including a small or an independent developer?

We'll also hear about what consumers, including gamers, think about loot boxes and concerns about how they are being marketed. To walk us through these issues, we will hear from representatives of two gaming industry associations and an attorney who represents companies in the video game industry. We also will hear from representatives of two consumer groups and from a talent agent who represents online performers and influencers in the video game space.

After lunch, we will turn to academic research by four professors, each of whom has approached the subject of loot boxes and digital media from a different angle. A media effects specialist will discuss his research on the associations between loot boxes and problem gaming. A marketing professor will present research exploring whether people who buy loot boxes do so to enjoy the game or to advance in the game.

An industrial engineering professor will talk about how to design and optimally price loot boxes from the perspective of the gaming company. We also will hear from a clinical child psychologist who helps parents and children address excessive and problematic digital media use. Our final panel of the day will examine what role self-regulatory initiatives in consumer education can play in addressing concerns about loot boxes and microtransactions.

You will hear from the organization that establishes ratings for video games, two consumer groups, and an organization that focuses on problem gambling. They will discuss video game ratings, tools that consumers can use to restrict or monitor in-game purchases, ways to improve consumer understanding and awareness, and suggestions for industry best practices. Our panellists today have a wealth of experience and represent a variety of viewpoints when it comes to loot boxes.

We look forward to a frank discussion of these issues and to using the information shared today and on the public docket to inform regulatory priorities, as well as industry and consumer guidance. We have a lot to cover. Before we do that, I want to single out a couple of folks for special thanks for organizing today's program-- Mary Johnson, Andrew Wone, Will Ducklow, Rick [INAUDIBLE], Patrick-- oh, Patrick, this is going to be tough-- McAlvanah, and Brittany Frassetto from our Bureau of Consumer Protection and our Bureau of Economics.

So without further ado, let me turn the podium over to Britney Frassetto and Andrew Wone to introduce the first panel. Thank you very much.

[APPLAUSE]

ANDREW WONE: OK. My name is Andrew Wone and I'm an attorney in the division of Advertising Practices. And co-moderating this panel with me is Brittany Frassetto, who's in our division of Financial Practices. The first panel today, as Andrew mentioned, is entitled "Treasure or Trifle, A Macro Look at Microtransactions." The panel will explore the role of loot boxes and similar mechanics in the video game ecosystem and the impact of these monetization models on end users.

You'll hear from six panellists who will present for approximately 15 minutes. After all of the presentations, we'll take a short break and then proceed with the moderated discussion. And now I'll turn the microphone over to Brittany who will introduce the panellists.

BRITTANY FRASSETTO: Good morning, everyone. So starting to my left and then going down the line is Sean Kane. Sean is a partner at the law firm of Frankfurt Kurnit Kline and Selz and is a founding member of the video game Bar Association. Next to him is Jeff Haynes, Senior Editor of Video Games and Websites at Common Sense Media. To his left is Mike Warnecke, Senior Policy Counsel for the Entertainment Software Association, or ESA.

Next is John Breyault, Vice President for Public Policy Telecommunications and Fraud at the National Consumers League. To his left is Renee Gittins, Executive Director of the International Game Developers Association. And finally, we have Omeed Dariani, the Co-founder and CEO

of Online Performers Group, which represents content creators in the video game space. And Sean will be starting us off this morning.

SEAN KANE: Thank you. Well, initially, I wanted to thank Mary, Will, Andrew, Brittany, and the rest of the FTC team for inviting me here this morning. So in a way, this is what I call somewhat my mandatory waffle slide. I'm here today really to speak about my own opinions. I've worked in the video gaming industry for over 15 years.

I represent more than 100 video game companies, and those companies range from literally one or two people that are creating apps for the app store all the way up to the largest video game publishers and developers in the world. I've literally wrote the book on video game law, so I was thankful to be able to come here today and just talk a little bit about my experience and try to give some background on the history of the games industry when it comes to monetization.

So I really wanted to start by just talking a little bit about where we've come because I don't think we can understand the modern concept of loot boxes and record transactions without understanding what the history of this industry looks like. So the games industry really became in the forefront of, I think, popular culture starting back in the 1970s. I was lucky enough to know the gentleman who basically created the home video game system, a gentleman named Ralph Baer who passed away a couple of years ago.

He created the first home game system back in the '60s. At the time, they really had no idea what they created and how it was going to really change popular culture. But once it was created, someone began to start to market it and they began to try to figure out, how can we build an industry around this? Initially, the industry really wasn't home-based.

I'm old enough to remember arcades. I spent many, many, many an hour and many a quarter playing games like Pac-Man and Galaga, and I did it fondly because there was a social aspect of it, there was an entertainment aspect of it. And these particular arcades were a place that people went to have community with like-minded individuals. And we played on very low tech games, and we pumped billions and billions of quarters into this industry.

If you look back on it and you adjusted for today's inflation, it's almost \$10 billion was pumped in by the end of the 1970s. But things changed. The consoles that we all went and used at arcades, in some cases, were still there. However, it was the dawn of really home video game systems. There was a shift. If we look at the late '70s into the '80s, there were more than a dozen home video game systems that were launched.

I will mention a few of them, and I'll be shocked if people remember some of these. But there was the Fairchild Channel F, which came out in 1976; RCA Studio 11, that's 1977; Bally Astrocade, 1977; my favorite and the one that I spent met too many hours on-- the Atari 2600, also 1977; the Magnavox Odyssey came out in '78; Intelelevision, 1980; and ColecoVision 1982. So the shift came from the concept of an arcade, a place that you would go to see these games, to the home.

Now initially, some of these games were more analog, they were actually built into the systems. So when you purchased that console, you pretty much got all of the games. That quickly changed. Games started to be sold on cartridges and disks as time went on. And those things replaced the concept of putting a quarter in every time you would play.

Now you were paying for those particular game that you wanted to play. No one was forced to buy all of them. You bought the game that you felt was going to be most interesting to you, most exciting to you, most entertaining to you. I spent a lot of time trying to jump over crocodiles in Pitfall because that was entertaining to me.

Now, in the '90s, we saw things shift even further because the technology increased, the bandwidth started to populate. We got to a point where you didn't necessarily have to go buy that disk, buy that cartridge. You can basically start, in a way, downloading certain games. And it was really a wonderful opportunity for hobbyists, people that liked games but wanted to actually create their own games. In fact, there are certain popular games that are out there today that really were launched as modifications to other existing games.

And so the downloadable aspect of games launched an entire culture of hobbyist gamers, many of whom stopped becoming hobbyist and became professionals. I'm sure Renee probably has many stories of people that started out modding games or started out creating their own simple games, and then have moved on to create other very popular games, both as independents or potentially going to move to one of the larger publishers or developers. But we also saw the PC market expand significantly as things like the PC culture in the US grew, Windows grew.

Now we get to the 2000s. This was interesting because PC games started to deal more with multiplayer issues. We started initially just with the LAN culture, which basically meant people were coming together and they were all plugging into a local network and they were all playing together in one space. Now, that changed and expanded to also internet-based multiplayer. So people didn't have to be in the same place. They could still be playing, they could still be socializing.

We also became, in the 2000s, the beginning of really browser-based games. Now, those were really some of the first free-to-play games. Before that, as I said, the games were sold individually. Now we have a rise of a business model where the games were free. You could go on, anyone could play them that had an internet connection. A lot of those games might have been backed by banner ads or other sort of advertising revenue models.

We also then launched into the arrival of really online multiplayer games. I think World of Warcraft is a great example of that. That was probably one of the first that most people, even those who weren't gamers-- weren't in the gaming culture, really had heard of. In that particular case, they would still sell the initial game, and then there was expansion packs or subscription models that survived out of that. And that's how the monetization was going for those mostly online multiplayer games. And it was really the debut of a subscription model-- people deciding that I'm going to play this game almost daily.

Prior to that, there were games that charged by the minute when you were playing or by the hour. That model changed and people started to realize, well, I can pay one set fee and play as much as I want over the course of a month or two months. I know people that have been playing World of Warcraft still for almost 15 years, and they have friends in the game and they have people that they consider family in the game which are part of their guilds or their clans.

Now we get into the late 2000s and we see the rise of the smartphones as game platforms. Initially, most of the games that were smartphone-based were pay-to-play. You spent \$0.99, you spent \$2, you spent \$4.99 to download that game, and then you were able to play that game as much as you want. But we also then had the concept of the freemium game, which, again, was a game that was free to play and anyone can play it. Whether or not you choose to spend or not spend is within your decision. And they're monetized by in-app microtransactions.

Some of the other panellists are going to really get into what the nature of some of these microtransactions are. So I'm not going to delve too much into them because I want to steal their thunder. But basically, what some of it was-- they were things like power-ups, they were things like extra live mechanisms. If there were cooldown timers built into the games, these were ways to bypass them.

Really, one of the first games to make the freemium model popular was a massively player online role playing game called Maple Story. It released in the US in 2005. So we've been seeing these things as part of our culture now for about 15 years. Once we get past the 2010s, we're getting into more of what the modern situation looks like in the gaming industry, and it is really more games as a service.

And they were designed basically to be workable when there was always an internet connection. Because some of the earlier mobile games, really you downloaded them. You could play them. You didn't need to have an internet connection, you didn't need to be connected in any way to the servers once you downloaded it really to continue to play those games. But now we have games that are much more interactive, and so that consistent connection is necessary.

These games have actually started to offer digital assets. These can be consumables and non-consumables. As the name would suggest, consumables are limited time-- maybe one use. They're something that you can use. Once you use it, it is gone. Non-consumable items, as was already mentioned, you have skins, you have different cosmetics, things that once you acquire, your characters, your avatars continue to use them. It allows for customization. And

I can tell you, as the son of a 14-year-old, customization in games is exceedingly popular and it's something that they do to really interact with their friends. They love to be able to show off some sort of new element that allows their game character to more reflect their own personality. And I think we live in a world right now where being able to reflect your personality is very important. So a new generation is finding new ways to do that.

But one of the things that's also come out of this now is loot boxes. And that's one of the reasons we're here to talk about. Loot boxes are interesting because loot boxes are not just things that are paid for. Loot boxes can be earned in-game as well. Most games have different sorts of

currencies, currencies that are earned and then currencies that can be purchased. And in many games, loot boxes can be accessed using either one of those currencies.

Now, the content of a loot box, in some respects-- they talked about surprise. That's a little bit of a misnomer. Not all loot boxes have a surprise element to them. There are definitely loot boxes where players have a very good sense, if not complete knowledge, of what's inside that loot box when they decide to open it. So certain games do have an element of them where there is an aspect of the unknown involving the loot box. But many other games make this known.

We also have things that have come out like battle passes and season passes. Now, these are somewhat similar, but battle passes, generally, we look at it from the context of you really know what's in that. You're buying a whole stream of content. It's known content. You have a very good sense of what each one of those things are. They'll be unlocked at different points in the game. So as you progress, as you play more, your account will unlock these different rewards. And those rewards can run the gamut from consumables, from skins, to wholly different aspects of the game that you can then play.

One of the first, I think, games that really had that was Valve's game Dota 2. Back in 2013, they released something called the compendium, which provided unique in-game content and features. So that was one of the first times we've seen these things. So we're looking at this now-- it's already been in the industry for over 6 years.

Now, season passes-- the concept behind there is usually more of a discounted package for current or future content. And that content, again, may be unknown. But again, it'll be unlocked as things progress. One of the games that really started that or put that out pretty early was Rockstar's LA Noire back in 2011. So again, that's another thing that's been around in the industry now for quite some time.

So one of the things I want to just hit before I run out of time here is, basically, games have really changed over the last 15 or 20 years. Really, these things were much more simplistic, they were linear. Now they're open worlds. If we look just at something like this, to see the changes just in the imagery of games has expanded to a level that's almost photorealistic.

But with that, the cost of games has skyrocketed. Over the last 15 years, your average AAA game, the cost has risen from, say, maybe \$20 to \$30 million to over \$100 million, and in some cases, over \$200 million. Because the cost of developing a game with hundreds if not thousands of hours of play, and then marketing that game is immense. We put together a slide chart just showing some of the costs of some of the top movies recently and putting them up against some of the top games-- the most expensive games to at least give a level of understanding.

And mobile games as well. My first mobile game deals were very small. They were \$5 million, a couple million, in some cases, a couple hundred thousand. And now they can be \$50 million or more because it's not just the development, it's the live operations of games that costs a lot for companies to create. A quick chart just to show some concept of if we looked at inflation, how much the cost of some of these games would have been even back when they were launched.

So the average game today costs about \$60. The average game in June of 2000 was about \$49. If we take that number and look at it for inflation, it really to be much, much higher. That \$49 would be worth about \$120.

But really, in the last 13 years or so, the price of games has not changed. The cost has gone up by about 1,000%, but the price of games has remained steady, which is why microtransactions has populated in the industry quite a lot. Freemium games, games as a service-- they went out there to stop piracy, but they also went out there to try to help bridge the gap between the cost of games and the sales price of games.

And I want to basically close by just saying some of the concepts of these microtransactions gives players a choice. No one is forced to spend money in a video game that is free to play. They choose what they want to spend and when they want to spend it and how they want to spend it. Effectively, it's a try before you buy model. You get to get out there and play a game. If you like the game and you want to spend money in the game, well, then do so. And the percentage that does is very small compared to the entire percentage of players in that particular game.

Microtransactions also means lower costs for everyone around the board and makes these things open to more people who may not have the ability to spend even \$60 right now. Or if we were going to charge the actual cost of development, that number might be more like \$300, \$400, \$500 a game to cover a budget of \$200 million. And it also provides parental oversight because, to the extent that people don't realize it, every one of the consoles has parental locks.

If parents choose, they can learn more about the consoles, they can learn more about the games their kids are playing. And they can make decisions on what games children should play and whether or not they should spend in it. I wanted to basically stop at that point and just say thank you again very much for having me. I'm happy to answer any questions that we have later on. And I will turn it back over to our wonderful FTC moderators.

ANDREW WONE: Thank you, Sean. Next, we'll hear from Jeff Haynes.

[APPLAUSE]

JEFF HAYNES: Good morning, ladies and gentlemen. My name is Jeff Haynes and I'm the senior editor of video games at Common Sense Media. It's an honor to be here today to talk about loot boxes, microtransactions, and advocating for consumers trying to navigate this digital landscape of games and apps. This is something that my writers and I deal with on a daily basis when we're evaluating the latest products that are released, so it's great to be able to share some of the expertise and insights on this digital content which might seem a little odd or confusing to some non-gamers. But don't worry because it's a little confusing at times to some gamers as well.

So to try to reduce this confusion, let's try to unpack loot boxes, shall we? So what are loot boxes? The simplest definition that could be used is that they're containers of randomized digital content that hold items of varying degrees of in-game value. That could cover everything from weapons and items to virtual cash, customizable costumes, game characters, and much more.

The rarity or associated value of each item within a loot box will vary from game to game and even from mode to mode. So that can make them somewhat unique.

It's also one of the reasons why they're known by many different names, like loot crates, price crates, booster packs, lock boxes, and many more. These are frequently earned rewards that are provided to gamers for their in-game play, and they often provide bonuses based on victories or particularly skilled moves demonstrated during a match. Loot boxes can also be purchased by gamers with in-game currency or with real money through in-game stores.

Now, unlike most video game genres, the current concept of loot boxes, as their thought of today, is still somewhat relatively new, having really developed over the past 15 years or so. They're descended from treasure chests that were typically found in playing games, like Diablo, or massively multiplayer online games, like World of Warcraft, and even earlier, things like Dungeons and Dragons. As players will complete quests, defeat bosses, or accomplish certain tasks, they'd be rewarded with chests that players could use to enhance and improve their in-game character.

But it was the inclusion of online access in games, as well as regularly updated content that helped drive the expansion of loot boxes from this niche feature to where they currently are today. Nowadays, loot boxes can be found in just about every single game genre, especially because developers made a heavy investment into these mechanics in the past decade. That being said, the genres that typically include these systems more than others are collectible card games, first person shooters, sports games, action titles, and role playing games.

But while loot boxes spread across multiple genres, not all of them were handled very well. Unfortunately, poorly implemented boxes raised a lot of user complaints and issues because some players felt that they had already paid for a game and were getting gimmicky play or were being squeezed for additional content that they had already paid for. Meaning that over a few years, a lot of complaints were being levied in forums and other locations. As a result, the video game industry started to move away from this as a response to consumer outrage.

As a matter of fact, at this past E3 a few months ago, a lot of developers were announcing that their upcoming games would not feature loot boxes or microtransactions. On the other hand, the mobile industry, which produces dozens of apps a week for phones and tablets, has fully embraced loot boxes as a way to additionally make some cash from consumers. Now, to help simplify some of the loot box distinctions, I'm going to group them into three categories. Before I break them down, I do want to point out something important.

Since developers can update and tweak the mechanics of these features at any point in time with a simple update, any or all of these categories could apply to a game with a loot box system at any point in time. So the first category is the cosmetic loot box, which typically provides optional content to gamers that they can choose to use or ignore for their gameplay. Cosmetic loot boxes don't provide an edge to players over their opponents, but instead, it gives them a ways to customize characters, weapons, and in-game expressions, which are also known as emotes. Those are the dances or the faces that are made that you often see in internet videos.

Games like Overwatch frequently indicated the kind of item that you received based on an easy to understand color scheme. The more colorful the item, the rarer the item happened to be. What's more, some games even let you redeem duplicate items to earn additional in-game currency, so that you could claim gear that you didn't actually have, which would reduce the amount of game time that you would have to play or even cash that you would spend on other content.

The second category are mode specific loot boxes. Now, these are usually tied to specific sections of games, like fantasy sports team management modes, and often use baseball card pack presentations to govern the provided content. By opening these packs, gamers acquire characters or athletes, gear, and items of varying quality. These can be used to build their teams or squads into the best possible lineup to play against online opponents or computer controlled teams. Duplicate items can be saved and used in later matches or sold for in-game credits in the game's auction house.

Now, on the plus side, this kind of loot box is entirely optional. You can avoid it entirely if you want to. But that said, some games will award in-game points for packs so slowly that it takes forever for players to actually acquire higher powered or rarer items. Star Wars Battlefront II is notorious for this, requiring the equivalent of days of consistent play to unlock one character or vehicle if players didn't spend real money to unlock them sooner.

The last category is sarcastically known as pay-to-loot, and it requires players to pay money to ultimately be successful with the gameplay. This typically occurs in collectible card games, like Hearthstone or Magic The Gathering in which players were willing to spend lots of money on higher tiered cards or packs, will frequently get a better chance of having more powerful units than other gamers. In other titles, like Call of Duty, Black Ops, some game modes, like blackout, even restrict access to certain types of year in the blackjack stashes unless you've already paid for them through the store.

In many cases, the options to unlock these items are limited, reduced, or removed, which leads to one of the biggest problems with the pay-to-loot mechanics. These are slot machine style mechanics, where paying extra possibly gives players more chances to earn higher rewards. But the developers control both the odds as well as the payout for these items. That tempts players into spending more money for additional chances to win rarer items, which could easily trigger people that have compulsive gambling urges.

But even people with restraint can find themselves in fiscal trouble thanks to a separate issue tied innately to loot boxes, which is that of microtransactions. It's important to note that while all loot boxes are microtransactions, not all microtransactions are loot boxes. But consumers that don't pay attention to how much they spend on these smaller purchases can quickly and surprisingly charge hundreds or even thousands of dollars on digital items. So let's quickly explore what these are.

Microtransactions are, in their most basic sense, optional virtual goods or downloadable content that can be added to any game for a nominal fee. These include expansion levels, new characters, enemies, game modes, and bonus items. One of the earliest examples of a microtransaction dates

back to 2006, where the Elder Scrolls IV, Oblivion offered gamers the chance to buy horse armor for in-game steeds for \$2.50. Nowadays, this content can be sold separately or even packaged together in bundles of like-themed content, such as costumes for characters or bonus materials to give players a head start in their titles.

It also covers what's known as season passes, which is something that Sean mentioned, which gives users a chance to buy upcoming content that will be released by a developer at a discounted price. Like loot boxes, these microtransactions can also be broken down into three main categories as well. The first is the optional microtransaction, which gives players the choice to include or exclude content as they see fit.

The one area where this gets a little bit dicey is when some games charge a little extra to unlock content that's already on a game disk or included in a downloadable title. Some fighting games, like Ultimate Marvel Versus Capcom, or role playing games, like Persona 5, kept content locked unless a purchased download code was recognized on a user's account. At which point, the game would reveal those bonus items. That tactic really wasn't popular with gamers and companies were frequently taken to task on the internet. So a lot of games have started to move away from this as a feature because of the negative response from the consumers.

The next kind are the pay to progress microtransactions. These are mainly baked into free to play games, where the basic game is free, but players are charged extra for incentives, in-game items, or to continue playing portions of games. Some people also refer to this as gatekeeping or metered play because developers can sometimes put arbitrary limits on gameplay, like limited turns, character energy, or limited moves that you have before you have to stop playing.

If you use up your allotted time, you're sometimes offered the chance to use in-game currency to buy more play. More than likely, you're basically urged to pay real world cash to get additional time sooner. Parents might recognize this tactic from games like Pokemon Go and Harry Potter, Wizards Unite, in which you're constantly controlled by how much energy you have to cast your spells or gather your Pokemon unless you go to real world locations to virtually check into areas, like gyms or inns that are designated by the game to gain additional power. Hidden object games also take this tactic by selling more time to solve additional puzzles.

The issues here are obvious. Metering the amount of available gameplay time might get some players to put the game down, but these limits don't always have a logical purpose aside from making additional money or slowing some players down that might fly through the available content within a game. Players with these games are also frequently hounded by in-game offers of extra energy or items for gameplay, prices of which can range from \$0.99 up to \$100 in some bundles. Worse, these games frequently include ads for other products to gain more time to play. This garners more cash for the developer because of the number of ads viewed, but it also allows them to gather info on the kinds of games that players are engaged in to serve up more ads.

Finally, there are the pay to win microtransactions, which is a variation of the free to play, or freemium, concept. The most successful games that use this approach, like Clash of Clans, Game of War, or Mobile Strike, tend to have very easy mechanics, which help to get players into the game experience quickly. These include detailed tutorials, colorful characters, and simple

controls. The difficulty level ramps up at a relatively slow pace, so players understand how the game play works and how to succeed.

Frequently, they offer a couple of practice rounds to build up your confidence about the single player experience, and then they add in multiplayer after a few rounds, which is where the bait and switch starts to occur because this is when they start to offer you the option to buy things to help you win. The problem with this is that instead of setting up a level playing field for all gamers, it blatantly skews the odds in favor of those players willing to pay for a clear advantage.

Players who are hardcore fans of the game that are willing to collect everything that is offered, players that have deep pockets or are willing to get themselves in financial trouble, and players looking for an unfair edge will always exploit these options instead of relying upon skill. Plus, these games frequently start by offering limited content for free and charging for more. Developers try to squeeze players in some cases as much as they can, while limiting access to new characters, content, or items in some cases, they might also restrict access to players who haven't chosen to buy certain items for certain game modes.

So how should consumers protect themselves from these issues? While not all of these are options that I'm going to give our foolproof and they can be limited in some scope, there are some steps that are available. First and foremost, consumers should realize that they don't really need to buy any of this content to play a game. There are plenty of great games out there that don't use loot boxes or microtransactions at all and others that include them as options instead of necessities to succeed. And if you feel that someone is getting greedy for your cash, as a developer, you can simply choose to delete the game.

It's also worth noting that free games seem to have most of the most problematic microtransactions and loot boxes. So easily, paying for games can help minimize some of these concerns. Being a paid customer also gives consumers a better position when it comes to complaining to companies. Both EA and Warner Brothers wound up changing their microtransaction formats in certain titles after players who bought those games had problems with some of the microtransaction and loot box mechanics.

And if you're a parent, you can also enable parental controls on devices to reduce the option of one-button payments. Or even better, you can remove the save payment information from your devices altogether. That way, anyone who's tempted to buy something will have to manually input purchasing info. For parents, this would reduce or eliminate surprise or sudden charges on their credit cards. And for other adults, it would provide a moment to step back and decide whether they really need to buy that downloadable content or if they can let it go for that day by itself.

Finally, parents can talk to their kids about why they feel that they have to have a certain item or want to spend money on a particular loot box. Not only can this help kids learn valuable monetary lessons, but it might further discussion about what makes a particular game so appealing. From there, parents can establish a plan or even a contract with kids which can cover everything from screen time limits on a particular game to purchasing sought after game items as a reward for doing well in school, say, or handling certain chores.

I hope I've been able to shed a little light on this complex topic with a quick overview of loot boxes and microtransactions. Thank you for your time and the opportunity to be here today. And I look forward to participating in the roundtable discussion on this topic and other pressing topics in gaming.

[APPLAUSE]

BRITTANY FRASSETTO: Thank you, Jeff. Next up, we'll hear from Mike Warnecke from ESA.

MIKE WARNECKE: Good morning. In my presentation today, I would like to share with you what loot boxes are, how they work, why they're in video games, and the steps that the video game industry has taken to make sure that consumers are informed and are able to make good purchase decisions about their gameplay experience. And with this, we hope to provide a good experience not only for consumers, but also to make sure that the wider consumer population is aware of the steps that the video game industry is taking in that regard.

So who is ESA? If you go into a Target or Best Buy and you look in the video game aisle, the people that publish those games are our members. We mostly represent the publishers of the AAA titles, the very popular games you play on your console systems, such as the ones on Microsoft, Sony, and Nintendo who are ESA members, as well as those that published for PCs. We also represent a few publishers in the freemium area, although that is a smaller part of ESA's membership.

So who plays video games? As was mentioned earlier today, most Americans do. In fact, about half the country does and about half of adults play video games. When I was growing up, one of my earliest experiences in playing video games was with my brother playing Sonic the Hedgehog on the Sega Genesis system. And back then, a game console was essentially a box with an AV cable. It didn't have internet connectivity. And it was a gift you would get from your parents for holidays or for birthday, and it was something you plugged into the TV.

It was essentially an elaborate toy, and that's what many parents viewed it as. It wasn't something that a lot of people played beyond a certain age. But flash forward to today and it's a much different situation. Today, the average gamer is 33 years old. And while kids are and always will be an important part of the demographic of our industry, they actually represent a smaller part than maybe people may realize. Only about less than a quarter of the game playing population is under 18. Most of the game paying population are adults.

So let's talk about what loot boxes are. Loot boxes are a game mechanic where players can obtain virtual items for use within the game. And the way it works is that the player may know the general type of item, but they don't know the specific item until they open the box. Now, if this sounds familiar, it's because it's a mechanic that we've seen before in other contexts. For 75 years or more, Americans have been opening up millions of packages of baseball cards to put together their dream team, to get the players that they root for on their home teams, and to build their collections with their friends. It's a common mechanic that people are very familiar with.

So why are loot boxes and in-game purchases in games? As Sean mentioned earlier, games today are not a static item anymore. They are constantly being refreshed and enhanced with online services. When I was a kid growing up and bought a game-- and back then it was Toys R Us, when that was a thing-- whatever that game was, good or bad, it was only going to be what was in that box. It was not going to be updated, it was not going to be enhanced. It was only what came in that box when you walked out of the store.

That is not the case today. Today, games are continually refreshed with new content, with online interactive features, with new experiences. And this is in response to what consumers want. When they get attached to a particular game, they want to continue to have new experiences with it and they want the publisher to keep it fresh and exciting. And microtransactions, such as loot boxes and other in-game purchases, help make that possible. Because there is a lot of back end infrastructure to make all that magic happen, so that when a consumer sits down to the game, they get a wonderful engaging experience.

And it's important to keep in mind, as Sean also mentioned, that pulling this off is really hard and really expensive. If you look at other forms of entertainment, such as reading a book or going to a movie, there's this concept called forced perspective, where you experience the world based on how the author or filmmaker is directing you to experience it. And that also, of course, applies in many video games.

But there's also another type of video game, and those are free world games where you can roam and explore the world all around you. And to be able to pull that off is really hard because you could wander from one territory to another, and you've got to create a credible virtual world that's believable and authentic and fun. And doing that involves a lot of people and involves a lot of time.

In fact, the production teams for these games can stretch into the hundreds of people and involve computer engineers, animators, programmers, historians, voiceover actors, writers. It just runs the gamut. In fact, some of our member companies have motion capture studios that rival that used in Hollywood, as motion capture is an important part of some of the high end animations that you will see in some games.

There's also the free-to-play market. It was the summer of 2007 and I was with some of my friends on the National Mall and we were sitting on the grass near the Washington Monument. And one of my friends turned to me and he pulled out his backpack and he showed me this black rectangle. He said, Mike, have you seen one of these? It was the first week that the Apple iPhone had come out and none of us had seen it. We were all excited. We looked at this thing with the colorful icons.

I don't think 12 years ago, any of us sitting around there on the lawn near the Washington Monument could have anticipated that free-to-play would be such a huge thing as it is today. It's important to note, though, that just because a game is free to play doesn't mean it's free to make. These games can cost millions and millions of dollars to make.

But the nice thing about free-to-play is it gives gamers another opportunity to experience gameplay. There was a demographic of people who would never play, who would never invest the time to figure out the controllers or want to get a game rig to be able to play PC games. But everyone can swipe left and right. And the simple controls that are on a mobile phone suddenly open up an opportunity for people to experience a lot of different games.

But what we also discovered, too, is that when people experience games, they want to be able to kick the tires on it and not get caught up in buying something until they have a chance to experience it. So that's one reason why we have these free mobile apps, where it gives you the opportunity to experience that, but also, you have the chance to expand the content if you decide to like it.

So what are some common misconceptions about loot boxes? One is myth one, players must buy loot boxes to play. That's not correct, they don't. Paid loot boxes are optional. You can get many of the same or comparable items through diligent game play or through direct purchase of in-game items.

Myth number two, all in-game purchases are loot boxes. As been mentioned earlier, that's not the case. Loot boxes are actually just one form of in-game purchase. And myth number three, loot boxes are unique to the video game industry. As I mentioned earlier, that underlying mechanic is common in baseball cards. And if you go to Amazon, there are literally hundreds of products that have a similar sort of underlying mechanism to them.

So what I'd like to do in this next part of the presentation is go through the mechanics of, OK, how do you get a loot box? What's it look like? And what's going on? And so what I'm going to do is walk through a few examples, and then hopefully after the end of that, you'll have a better idea.

So loot boxes, you can acquire-- you can purchase loot boxes and basically two key ways, one is with money and the other is with in-game currency. With money, it may be, say, you're playing a free-to-play game. There's the loot box opportunity. It'll be a pop-up-- do you want to spend \$0.99 to get a loot box? You hit, Yes, and then it goes ahead and your app store account will be debited for that amount.

Now, another approach is with in-game currency. And with this approach, the publisher essentially sells a bucket of play money to the user, and then the user uses that play money to acquire items within the game. And there are a couple of practical reasons for why it's done this way. One is, it would be impractical every time someone does a \$0.99 or a \$1 transaction, to have that go to their account because it just would be annoying to have that constantly happen if you wanted to buy a few of them and to deal with all that.

And also, for the publisher. The transaction cost, if credit cards are getting used, would be significant if every time there was a small transaction like that, that that was a new transaction. But there's another reason, too, and that's to preserve narrative integrity. When you have a game, our members try to create games that are engaging and that are true to their world.

It would be very weird-- for instance, say you had a game set in ancient Egypt and you wanted to buy a chariot for a big combat that was going to come up and you went to the marketplace in Thebes. You would not want to be buying a chariot for \$2.50 US. It would be a little bit jolting and a little bit odd. So instead, the publisher will make it with a historically appropriate currency, such as a debin of copper, which would fit in more with the narrative of the game.

So what I'd like to do now is walk through a few examples of loot boxes in the wild, so you can see what that experience would look like. So the first game is MLB, The Show '19 by Sony Interactive Entertainment. It takes America's favorite pastime, baseball, and provides you the opportunity to manage your own baseball team and all the fun that goes with that, from selecting your manager to building your roster to deciding what features your stadium may have. And in this game, there is an opportunity to get digital packs. And these digital packs allow you to build out your roster. They're not the only way, but they're one way.

And so here's an example of-- I'll show how it works a little bit, and then you'll see a video briefly to see the walkthrough. So we're going select this pack, and you can see it says S 1500 and that's for stubs, the in-game currency. So if you select that, you can go ahead and then you can see on the far side-- you see what we call in the industry drop rates-- you can see the ratios or the probabilities of getting certain players. And the players that are more desirable, the diamond level, those would be a little bit harder to get than the ones who are more common.

OK. And so you go ahead and select it. And you can also see right next to that there's another button you could push to get the odds disclosure as well. So there's multiple ways of getting that information. It asks if you want to confirm the purchase. You indicate, Yes. And then there you go, the digital pack, you've now acquired it. And it's showing you what you've got, and then you can go ahead and open it. And there, you see the cards you have, and the flip side of that card, you can see the player's stats.

And also, you can see there's an opportunity there to sell it for in-game currency or go to the marketplace. And what that means is basically, one of the features of the game is you can go ahead and trade cards within the contours of the game-- within the game space, not going outside of it, to build your team. And so that's a feature of this particular game. And now we'll see a short video of that in play.

So this next one is Forza Street, a game by Microsoft for Windows 10, and it's a racing game. And as you can imagine with a racing game, one of the cool features is being able to acquire a vehicle or upgrade your vehicle to do new things and different things and to impress your other friends in the game. And so there's a mechanic in the game that allows you to-- what are called spins, where you can get a new car for use in the game. And you can use the in-game currency to acquire these spins. And so we'll see an example of what that looks like now.

You can see at the end there where the car, it will indicate what you're getting when you get the spin or what it costs. And then here we go with the selection process. And there we are. I'd gladly trade my old Honda Civic for that car. Maybe Microsoft can help me with that. So this last example is from The Sims, which is an iconic property in the video game industry. It's been around for nearly two decades and it's a game where you can become whoever you want to be

online and, basically, just go through daily life with other avatars. And it allows for a lot of personalization.

And one of the charming features of this game is Izzy's Design Studio, where he will help you look fabulous through developing an outfit for you. And one of the ways he can do that is through new designs. And basically, this uses a similar mechanic to a loot box. It's not a loot box, but it has the same underlying aspect of buying an opportunity to get content that you know the general type of, but not the specific item until you go forward. So here you can create a new design. And if you click on the question mark there, it'll show you the probability rates of getting various items of rarity.

And then we go ahead with the design. And there you go. You could see the fabric and the type of article of clothing, some stars to add some decoration. And then that other thumbs up is for a power or attribute that would apply to the clothing. And if you decide you'd like some of the clothing but you-- oh, and also, you can see the color bars in there to indicate the probability levels in terms of how rare the item is. Now, you can decide that you want to-- maybe you don't like that and you want to keep the dress, but you want to get some other articles or the other features you want changed. You can then get another design with these fashion gems and go ahead from there.

So in the last part of my presentation, I would like to talk about transparency and control and what the video game industry is doing to help ensure that consumers have a good game play purchase experience and to provide them the information they want as to what in-game transactions they encounter. Now, a little bit later this afternoon, Pat Vance from the ESRB will be going into some of this in a little more detail, particularly the in-game purchases label. But I think it's useful to lay out a little bit of this now, given the conversations we're going to be having between now and then.

So ESRB is the game industry's rating authority. And besides having the age ratings, they also provide a number of enhancements to the information they provide to help parents make informed purchase decisions. And last year, they rolled out the in-game purchases label. And basically what this is is if a game has microtransactions and if there's money you spend postgame on things within the game, this in-game purchases label would be disclosed on the box or when you download the game. So it's a signal to parents, for this may be something that they might be interested in.

Now, this ties in very well with the spending control features that are on the game consoles. All three of the game consoles have the ability to set spending controls. And that may include, for instance, setting a limit on the amount or blocking purchasing altogether. In addition to the game consoles, I should also note that EA's Origin platform for PC games also has spending control features. And one of the interesting features of the EA approach is that in addition to being able to create a child account, you can also create a separate account for a player account, for instance, for older users, if you want to set spending limits for those individuals.

That said, we are doing more. I'm pleased to announce this morning that Microsoft, Nintendo, and Sony have indicated to ESA a commitment to new platform policies with respect to the use

of paid loot boxes in games that are developed for their platform. Specifically, this would apply to new games and game updates that add loot box features and it would require the disclosure of the relative rarity or probabilities of obtaining randomized virtual items in games that are available on their platforms.

As well, many of the leading video game publishers of the Entertainment Software Association have decided that they are going to implement a similar approach at the publisher level to provide consumers this information and to give them enhanced information to make purchase decisions. And many of the features of those two approaches are quite similar. Again, they would play to new games and game updates and they would require the disclosure of the odds of the relative probabilities.

Now, this approach would also be compatible with the Apple and Google approach on the mobile platform. And we believe that taken together, this provides a comprehensive approach to ensuring that consumers get the information they need so they can make informed purchase decisions when it comes to paid loot boxes. Thank you for your time.

[APPLAUSE]

ANDREW WONE: Thank you, Mike. Next, we'll hear from John Breyault from the National Consumers League.

JOHN BREYAULT: Good morning. Just like to add my thanks to the Federal Trade Commission for putting together today's event and for inviting NCL to be a part of this event. So the title of my presentation is called "Making Money From GAAS, or Games As A Service." And I would like to talk about consumer protection priorities and issues that we'd like to see the Federal Trade Commission explore. So as was mentioned, I'm with the National Consumers League. I handle our tech and telecom advocacy portfolio.

But NCL has been around for 120 years. And our mission focuses on everything from food safety, health care, child labor-- you name it, NCL has probably advocated it for it at some time or another. And this probably dates me, but I have been a gamer since my first console, which was the Atari 2600. And so this gives you some idea of how long I've been playing games.

So are what we going to look at today? First of all, we're going to look at, what are games as a service? We're going to talk about the scale of microtransactions you've been hearing a lot about from my other panellists. We're going to explore some ways that monetization of games as a service can become predatory, explore some of the concerns we have around the use of in-game currency. And then we'll turn to eSports streaming and how that relates to the FTC's endorsement guide. And finally, we'll talk about some questions that we hope the FTC will explore as it continues to look into this matter.

So first off, what are games as a service? This is a slide helpfully provided by Ubisoft, which is one of the big game publishing houses, in their earnings slides. First of all, in the past, games were hit-driven and cyclical. You saw a few games came out that were big hits and others that were flops. But typically, consumers would play with them for a few months, and then move on

to the next game. What you have now is a recurring revenue business where there are opportunities for recurring purchases through microtransactions, through season passes, et cetera that you've heard about.

In the past, there was low user engagement. The players weren't really interacting between themselves, they weren't engaging on Twitch streams, you didn't have eSports leagues. Today, you have high user engagement where consumers are doing all of these things. You had a console focus. Many of us can remember fondly opening up on Christmas morning that NES, or Sega Genesis in my case, and that was how you experience games. Well, today, the game is a multi-platform business.

I was at a barbecue on Saturday night with some friends and there was 10 kids or so playing Minecraft with each other. Some of them were on the console, one of them was on the PC, the others were on their mobile devices, and they were all playing the same game. That's emblematic of how the multi-platform business model has evolved. We went from being a developer-centric industry, where basically you had developers have a vision for a game and they spend however long they're going to do to develop the game and they put it out there and hope it's a hit.

Today, you have a player-centric model, where the games are being driven by feedback from gameplay itself, from attention paid by publishers and developers to the chatter around these games online. And then they are using that to iterate on the game after it's already been shipped. You went from having an experience where you basically interacted with the game itself to a platform experience, where most of the interactions, purchasing of payments, et cetera are managed by the platforms, the Xboxes and Playstations and Google's and iOSs of the world, not necessarily the publishers.

And finally, the success of games used to be calculated in terms of the number of units ships. Today, they're being evaluated by the lifetime value. So not only how much you pay to acquire the game, or in the case of free-to-play games, not at all, but then how much value is delivered over the life of the game through things like microtransactions. And these are measured in years, not months. So let's talk a little bit about the scale of microtransactions.

This is some research from Juniper Research, who had a very helpful paper called "In-Game Gambling, The Next Cash Cow for Publishers" that came out last year. But total spending on loot boxes and skin gambling is forecast to go up to \$50 billion by 2022, and that's nearly doubling since last year. The chart on the right shows you breakdowns in recurring investment as a percentage of total sales from three of the biggest publishers out there, Ubisoft, EA, and Activision Blizzard.

And the yellow part of those charts shows you how much is coming in from player recurring investment. This is the money that consumers pay after they've already acquired the game through loot boxes and microtransactions and other events. You can see that it makes up a very substantial portion of the money that they have coming in. And this is just additional data supporting that point. On the left, you have EA's net bookings for Q4 2018. And you can see the green part of that chart is the live services, the bookings they're getting from microtransactions and et cetera.

And you can see that it's grown now for EA to 31% of net bookings just over the past three years. Similarly with Ubisoft, you can see it's the purple part of that chart, which shows that these sort of recurring purchases are generating about 69% of their digital split and net bookings. And Activision Blizzard, it's very similar. It's not shown here, but nearly 70% of their FY 2018 net revenue came from non-product sales revenue, microtransactions, DLC, World of Warcraft subscriptions, et cetera.

Unsurprisingly, this shift away from that old business model I've talked about earlier to the new business model of games as the service has been incredibly profitable. What you see here is the percentage of EBIT margin for four of the biggest publishers out there, Ubisoft, EA, Take-Two, and Activision, since 2005. So you can see in the first part of this chart that cyclical business model I was talking about. And then what you see is in 2010 a shift to an unbroken line and increase in profitability.

Unsurprisingly, that was when one of the biggest multiplayer games out there, Team Fortress 2, started to employ loot box mechanics in North America and Europe. So we've established now that it's a changing industry, that this shift to games as a service has been very good for the industry. So the question is, when does this become predatory? So here in the next few slides, I'm going to apologize because I'm violating the cardinal rule of PowerPoint by putting up word-dense slides. But this is research from Dr. Daniel King and Professor Paul Delfabbro at the University of Adelaide in Australia.

And I direct your attention to the highlighted sections, which talks about how in-game modernisation schemes can become predatory. They are talking about how they can often be used to disguise the true long term cost of microtransactions until the player has been financially and psychologically committed to a game. And these monetization schemes are often enabled by information asymmetry between the players and the industry regarding things like game related preferences, how much money a consumer may have spent in the past, their spending habits.

And another sign on this again is how player data may be used to manipulate the nature and presentation of purchasing offers. For example, publishers in the industry often talk about having a whale. This is someone who is likely to spend a significant amount of money or who has spent a significant amount of money on the game. And so what's unclear is whether that data on how players are likely to spend more money is being used to do things like manipulate odds on loot box drop rates.

So particularly concerning to us is how this kind of information asymmetry is affecting younger players who may be less equipped to accurately apprise the value proposition of such schemes. So now you may be wondering, well, so what? This is so what slide. It's based on research from David Zendle at York St. John University, who you'll be hearing from later on today. But again, the highlighted portion talks about the reason that these monetization schemes can become predatory.

So, for example, his research has found that older adolescents who spend money on loot boxes may be twice as high to show measurements of problem gambling and that when you are exposed to problem gambling earlier in life, this can lead to potentially negative consequences

down the line. So I'd like to turn now to a specific issue that we're looking at, which is the use of in-game currency. As you've heard from the other panellists, in-game currency has proliferated throughout the top games.

In FIFA, you've got FIFA coins. In NBA 2K 19, you've got VC. In Overwatch, you've got credits. In Fortnite, you've got V-Bucks. In Call of Duty Black Ops 3, you've got Call of Duty points. So the currencies obtained via gameplay or purchase, our concern is that they may obscure the true cost of purchasing in-game content. So does it actually tell you how much you're spending in real money down the line?

So this is a screenshot from the store in Fortnite. And what I direct you to is some of the common psychological tricks that you may have seen before in the retail context. When something's priced at \$1.99, you may not think that this is \$2 and be more likely to spend money on it. This is used throughout Fortnite and I think you see this in other games as well. The problem here is that when you combine this with things like these bonuses that are offered here, it puts a lot of cognitive load on the user, creating a complex exchange rate between digital money and real dollars.

And it can make it easy to lose track of an object's real world value. Sorry, go back. So other features that I think have been mentioned a couple times in the panel already that are concerning to us are ones that may make it more difficult or frustrating, such as time investments, if you've lost your last life, take something that initially took seconds, like building a new structure in a game, may stretch in the minutes or hours, and it may be impossible to beat the game or even advance without spending money.

So now that we've talked a little bit about our concerns around the use of in-game currency, I want to turn really quickly to eSports streaming and the FTC's endorsement guides. So as you can see from the chart, the eSports market revenue has become more than a billion dollar business. By 2022, it's expected that it's going to go to \$1.8 billion dollars.

This is from Newzoo. And in 2017, the FTC did bring enforcement actions against two influencers who were using their YouTube Gaming channel to endorse a skin trading site called CSGO Lotto without disclosing that they actually own CSGO Lotto. So this is important to look at in what has happened since. The eSports market has continued to explode.

You see some of the biggest events, like the IEM Katowice and CSGO tournaments who are attracting tens of millions or hundreds millions of viewers. And this is comparable in some cases to what we're seeing for traditional professional sports. The NBA 2018 finals averaged around \$17.7 million, and we're starting to approach Super Bowl levels of interest.

And this is just some additional data on that point. This chart shows the peak viewerships in July for the top 10 Twitch streamers. We're talking between 150,000 and 300,000 viewers of those Twitch streams at any one point. And this is, unsurprisingly, generating big money. So these headlines speak for themselves. And much of the money that is being able to fund these streamers and these events is being generated through money that is being spent by players in microtransactions.

And so in our admittedly unscientific review of top streamers content for games like Apex Legends and Fortnite, we rarely heard any of them disclosing connections to the publishers. Even in videos where essentially they were showing off that they were opening loot boxes and getting reactions to that, we did not see evidence where streamers were saying, I was given money to buy these loot boxes by a publisher. So the question is, how are they getting all the money to buy these loot boxes? And is this being adequately disclosed in compliance with the FTC's endorsement guide?

So I'd like to now turn to some key questions here. Admittedly, there's probably still more unknowns than knowns when it comes to whether and how any of the practices that I've described in this presentation can or should be regulated by the FTC or Congress or anyone else. But I do think that the evidence that's been presented raises a lot of key questions that we think is appropriate for the FTC to investigate. So first of all, are loot box odds being manipulated to incentivize continued play and eventual monetization?

I think it's important to put this in context against the baseball card examples that several of my previous panellists have mentioned. When I buy a Magic the Gathering pack or a baseball card pack at Target, my odds of getting a rookie card or a rare card there are fixed-- it's a physical thing. But when you're opening loot boxes online, those odds can be manipulated based on a variety of factors. If that is indeed the case, what factors are being used to influence loot box drop odds? Is it things like data on how players are playing the game, how many available funds they may have in their account, whether they've purchased things in the past?

Does disclosure of the loot box drop odds influence player behavior? I was very pleased to hear Michael talk about the announcements about disclosing loot drop box ads. I'm going to be very interested to see if data comes out after that about whether that disclosure of such odds is influencing player behavior. With regards to in-game currency, I think it's important to look at whether the disclosure of cumulative in-game spend in a currency that consumers actually understand would address some of the concerns we raised around the difficult exchange rates and the cognitive load that is put on consumers.

And finally, I think it's important, even though the FTC has taken a look at this issue to some extent in the past, as the eSports marketplace continues to explode-- I don't think anybody is predicting that it won't-- are the leagues, the publishers, and the top streamers complying with the FTC's enforcement guide? Thank you very much.

[APPLAUSE]

BRITTANY FRASSETTO: Thank you, John. Next up is Renee Gittins from IGDA.

RENEE GITTINS: Hi. So my name is Renee Gittins, and I'm the executive director of the International Game Developers Association. The IGDA is the largest non-profit membership organization representing game developers in the world. And our mission is to support and empower game developers in having fulfilling and sustainable careers. I myself am also a game developer. I have expertise in creative direction in engineering, and, of course, I'm a gamer as well.

Like our other panellists, I want to help you understand what a loot box is. Unfortunately, there's actually quite a large range of possible variations of what you can interpret a loot box being. Generally, it is considered a consumable item, a single use item in a video game that contains randomized rewards. However, as you'll see from my next few slides, there's a huge range of items and mechanics that can fall under the term loot box.

First, let's look at different ways to acquire these loot boxes. They can be directly purchased for real money. They can be potentially purchased for in-game currency that is either earned or bought. They can also be rewarded for accomplishing feats, for playing the game, for logging in regularly. Once you achieve one of these loot boxes, they can provide various rewards.

These include cosmetics that have no effect on gameplay but provide visual benefits; content, such as mechanically unique characters or access to game modes; consumables, which are items that can be used, such as experience boosts, health potions, and other usable items; upgrades that change the gameplay and your ability within it, such as weapons and armor; and finally, they can also contain in-game currency, or duplicate items or items you do not want may be traded for in-game currency.

Once you obtain these loot box contents, games handle what you can do with them differently. Some of these contents are locked to your account. You can no longer sell or trade them once you acquire them. Other games allow you to trade these to others, either as gifts or for exchange of other items or in-game currency. Some games, in fact, allow you to trade some of these items for real money as well. And some of them have limitations on when these items can be traded, if at all.

When you look at these number of variations-- and this was just a few that I listed-- you will find that with these different types, there might be a number of combinations. At first you might think it's, well, a few hundred. But when you give it a rough statistical analysis, it's closer to 52 million different types of combinations of what could be considered a loot box.

Here's an example of complexity in loot boxes in a popular game. This game has two types of loot boxes. One of these loot boxes can be acquired by purchasing an in-game item that gives you access to a progression. This progression has various rewards, including loot boxes along the progression chain.

Progress on this chain can also be directly purchased. This game also has a second type of loot box. This loot box is only available through event participation, is provided at random, and cannot be earned or ground out by expanding multiple hours or by spending any money. Both of these loot boxes provide permanent cosmetic rewards and ensure that you do not receive duplicate rewards.

This game also allows you to sell the loot that you acquire in the second box, which you can not directly purchase. However, the cosmetic items that you achieve through the purchased loot box or the indirectly purchased loot box are completely account bound and cannot be traded or sold to other players. Both of the loot boxes do not allow you to have any other method of acquiring that content.

This shows how in a single game, there can be multiple uses of things which would be considered loot boxes, even though they have different mechanics. As you can see, this quickly becomes a very complicated space. There are many similar mechanics in games that may be considered loot boxes or perhaps fall under incorrect loot box definitions. As noted by other panellists, loot drops, randomized rewards, are very common in video games and have existed since 1980.

In fact, random rewards for achievements in games have been in existence prior to video games in pen and paper games as well. And of course, we have seen randomized rewards and physical items as well. Now, there are monetary motivations for adding loot boxes and other microtransactions. Games have cost approximately the same amount for many decades. The average game price has been about \$60 for the last two decades. And when you're looking back at game prices in the 1970s, you'll see that with inflation, that would cost well over \$200 today.

Game development costs, consumer expectations, and team sizes have grown greatly. As cost of living expenses have increased, game developers require better payments to maintain their daily lives. Also, with the growth of mobile games, we have seen that almost 50% of global game revenue comes from mobile games. Consumers do not generally support upfront purchases in mobile games or in any other mobile apps at all. Thus, most mobile apps allow for microtransactions, and that is how they pay the development teams. And here's a graph, as you can see, the comparison of average game price over time with it adjusted for inflation.

Implementation costs of changes to any game system can be expensive. If there were to be changes required for game developers, it could affect game development teams, both by requiring them to spend time and effort changing games, but also affecting consumers that work in these established in-game economies. When you've played a game and invested time, money, or emotions in it, having outside changes influence what you've invested in can be a disrupting experience.

While large game developers can react rapidly to required changes, small game developers suffer. In fact, I know many developers who released mobile apps on a very quick cadence, and then live off of the backlog of those games slowly trickling in money. If any changes that are made require them to change all of their previous games, then that would cut off their income and require months of development for them to get back on track.

We can also note that there are current protections in place to prevent children from interacting with these loot boxes and other in-game purchases. I know that children are a deep concern, particularly for vulnerability, but I think that we've done a very good job in providing protections for them. First, we have COPPA, the Children's Online Privacy Protection Act. This prevents children from under the age of 13 years old for making an account which loot boxes can even be credited.

Additionally, online purchases and in-game purchases generally require credit cards, which require you to be an adult, or other 18 plus accounts, such as PayPal. While there is an exception, such as gift cards, these are not as popular and require other outside of online and in-game

purchases to acquire. Finally, as noted by other panellists, app stores and consoles have store parent controls.

I would like to share some game developer opinions on this subject. Game developers are a wide range of people. Some of them support loot boxes and some of them do not. Some of them love loot boxes as gamers and some feel frustrated by them. I would like to share two opinions on either end of the spectrum. The first will be from someone who supports regulation on loot boxes and the latter will be from someone who opposes it.

Here's the first. "Unfortunately, it seems that the industry is having trouble being ethical when there's profit to be made. If someone cannot be trusted to not exploit someone else, then we must place down a regulation to protect others." Here's the second statement. "I do not think it is the government's role to regulate. It should be the industry and consumers that do. It could be a slippery slope that could lead to game censorship, since the gaming industry has and will always be an easy scapegoat."

In summary, game development is a complex space and loot boxes and transactions can span a wide range of definitions. There is also a large overlap between loot boxes and established random reward game mechanics that have been present even before video games. Monetization, including microtransactions, has been driven by inflation and increasing player willingness to make upfront payments, particularly on mobile platforms. And there are current protections that guard children from microtransactions and loot box abuse.

Finally, game developers are worried about heavy-handed regulation hurting the game industry and their creativity. In November 2018, the IGDA recommended and continues to recommend industry self-regulation combined with proper enforcement of current regulations and protections. We recommended that game studios confirm a commitment to not market loot boxes to children, that they clearly disclose odds of different rewards, and that they work to educate parents on parental controls available.

We are proud that the industry has begun to heed these recommendations. I would like to note that game developers, in general, are very passionate people that are working on creating art. I know many game developers, and as a game developer myself, I know that we are interested in exploring empathy and providing emotions to our game players. While there are different monetization strategies, game developers in the end just want to provide joyful and satisfying experiences that make people experience something new in this wonderful medium of games. Thank you.

[APPLAUSE]

ANDREW WONE: Thank you, Renee. Now we'll hear from Omeed Dariani of the Online Performers Group.

OMEED DARIANI: Hello. Oh, yeah, there it is. So my presentation's a bit different than everyone else's today. Let me tell you a bit about my company and why I'm here. So Online Performers Group is a company that represents content creators. We represent content creators

across Twitch.TV, Mixer, YouTube, Facebook, Caffeine. Basically, anywhere that people are playing games and interacting with live content, the talent that's there, we're helping them.

So a few of the clients that we manage are on the screen. They're a very interesting group of folks, including people like C0hnc4rn4ge, T-Pain-- who does not like to be called rapper T-Pain, by the way-- the heavy metal band DragonForce, professional baseball player Trevor May, and the Angry Joe Show. In total, we represent about 70 content creators who have over 50 million followers. And each day viewers watch over 60 years of content created by these folks.

So these folks do a tremendous amount of work showing games to people and talking about the game industry, in general. Some notes-- we work for content creators. I've worked in the game industry for a long time myself, but we work for content creators exclusively. We don't take money from game companies. We don't accept direct compensation from game companies. Our clients do. We're paid by our clients. Our main goals in the industry are fighting the exploitation of content creators and improving the game industry and creating transparency.

So why are we here? So we represent content creators, and in many ways, content creators represent the gaming community. So content creators are a fairly new phenomenon in the industry and they're fans. They start as fans of games, they love games, and their work is born out of that love. And because of that-- because of their talent and entertainment value, they gather a following. They gather people who are like-minded and interested in what they have to say. And as they develop, they often become opinion leaders or critics or advocates of the industry.

And because of the unique place they sit in the game industry, they're able to speak their opinion very clearly and very transparently. What's really interesting to me, as someone who's worked in the game industry for about 20 years, is that they're making the game industry better. For a long time, the game industry hasn't had a really great way to connect directly with their fans. There's lots of fans, lots of people consuming games. But because these content creators marshal millions of fans to one place and their fans tend to agree with them, they become great advocates that can speak directly to game companies.

So why we're here today talking about loot boxes is because of some controversy surrounding them. And in many ways, this controversy started with content creators. Content creators, like Angry Joe, who have long been critical of practices that they feel are predatory or not in the best interests of the gaming community feel a very personal stake in protecting and advocating for content creators. Star Wars Battlefront 2 was a flashpoint for this last year. And the outrage around that really brought focus to this issue.

And what's really interesting to me is this isn't just some angry guy shouting on the internet. People like Angry Joe were able to make change. Very shortly after this video and after this discussion started, EA vowed never to put paid loot boxes in Star Wars Battlefront 2. And as you can see, this is what Joe had to say about that. What I think is most interesting about Joe's statement is "we will be keeping an eye on these practices," "giving us what we suggested." He's speaking for the community. That's what he believes and that's what his fans want him to do.

So we've got a lot of fantastic people, and I thank everyone on the panel for their contributions and everything wonderful that's been said and will be said later today. We have great advocacy organizations here, but we don't really have a group representing the gaming community. And so I've been asked-- which is a really tall order-- to represent the gaming community on this panel. Now, the first thing I want to say is the gaming community is huge. Over half of Americans play games.

Virtually everyone plays games. So as you can imagine, the gaming community covers every group of people, every age, every socioeconomic group, everything you can imagine. And as you can imagine, they don't all agree. So there are a lot of different viewpoints here, and throughout these slides, I'm going to show you a lot of direct feedback that I've gotten asking questions and talking to people, both through Twitter and through email.

The community wants to be heard. Now, the number one thing that I've heard probably in my career in dealing with the community is they don't feel like game companies listen to them. So you can see from these Google auto completes when people are searching for Blizzard-- Blizzard doesn't care, Blizzard doesn't care about customers, EA doesn't understand, EA doesn't care, EA doesn't deserve Star Wars-- ouch. But really, there's a lot of frustration in this issue from the game community and it stems from the fact that people don't believe game companies listen to them.

Having worked at game companies, I know that game companies try to listen to them, but it doesn't always feel that way. The community mostly thinks loot boxes are gambling. So of the feedback that I got-- there was a wide variety-- but over and over, we had people coming back to this idea that if it's not gambling, it feels like gambling.

So even though I think we can pretty clearly say that loot boxes are not exactly the same thing as entering the lottery, not the same thing as sitting in front of a slot machine, they do have some of the same feelings that gambling does. And so even though it's not gambling, it does feel like what I'm calling gambling within a game system.

The community wants to keep kids safe. People, they like kids. And a lot of the opinions here are rooted in the fact that we see easy opportunities for kids to be taken advantage of. And these are a couple of stories from the BBC talking about exploitation of kids or kids just spending way too much money in games. And I think one of the real reasons that this hits home is, as a parent, you can't watch every minute of every show that your kid watches, you can't sit there while they play every minute of every game.

So you're making your decisions on the front end. You're looking at the box, you're looking at the rating, you're looking at the review, and you're saying, OK, this is fine. But then the moment where these sorts of stories happen is inside the game. So it's at a time that the parent can't necessarily be there. And obviously, there are controls for this, but the sensitivity of this kind of thing happening is there. So people are very concerned about that.

This is actually an email I received from a guy in Germany. I thought it was really interesting because it really talks through the entire process of the pressures surrounding people. So as was

mentioned earlier, a lot of these microtransactions and loot boxes happen in online games. Online games are both competitive and collaborative. And so what he's talking about here that's really interesting is the collaborative nature of pressure.

So in being in a clan or a guild, something like that, he wants to do right by the guild. He wants to hold up his end of the team, that sort of thing. To do that, obviously, you need the best equipment, you need to have everything that the highly competitive people have. And of course, a lot of those things end up in loot boxes or end up in the ultra premium packages. So because of the scope of these, which has been talked about as well, you can see how this pressure comes both from wanting to be the best, but also not wanting to let your friends down.

The community wants to get what they paid for. Now, we've heard about the horse armor already, but I think this illustration from Forbes really nails the feeling that the game community has. When most of us started buying games, there was this covenant. I buy the box, I get what's in the box. That's the game. Maybe there's an expansion, maybe there's something like that. But ultimately, I know what I'm paying for. I don't have to go out and make an additional purchase or I'm not going to be consistently monetized.

So there's already this feeling that comes along with that that is pretty negative. And I think that horse armor really kicked us off on the wrong foot because the DLC was included on the disk in some cases, which meant you were literally just paying to unlock something that you already physically owned. And as we can see-- it's a quick progression here. I know a lot of this has been covered already, so I won't talk too much about it.

But the way we got to today was not overnight. You had these microtransactions normalizing through a lot of different games, through a lot of different platforms. They went from console and online games to Facebook, social media games. Everyone remembers the amount of Farmville spam that used to appear in our feeds. And then when we hit social media, we have a lot more refined ability to monetize people, which has led us here to Star Wars Battlefront 2 and the other modern games we're talking about. Definitely applaud the ESA for that announcement from Sony, Microsoft, and Nintendo as well. That's really exciting.

The community, they want regulation of loot boxes. So there's a lot of discussion about, how does this happen? One of the things that's really interesting is there's a break between mobile games and other video games. They're regulated in different spots and so far have not been very consistent. So the people that are frustrated, they also have concerns about government regulation, as our first friend has to say here. But realistically, people are looking for some more structure, they're looking for some more guidance. They want there to be more definition around this topic.

Now, what do I think? Well, we've touched on this a lot, but I think that all of these things feel like gambling. I've played Magic my whole life, I collected baseball cards, I bought those stupid eggs, every one of those things. But they are all the same search. I'm looking for that rare thing, that special thing. With the exception of-- there's the true surprise mechanic there with the Cracker Jacks. That was the last time I felt like any of these were a surprise mechanic. When I opened a pack of Magic cards or pack of baseball cards, I know exactly what I'm looking for.

Now, how do we go forward from here? Well, this is a pretty complicated issue, as you've seen. And there are several things that are standing in the way of good regulation here. The first one is that the government doesn't tend to understand games and technology very well. Our elected officials are old. The average congressperson was born in 1961. So that's years before the Atari 2600, 37 years before Google was invented. For a kid who grows up today, Google is just part of your life.

The president is six years older than Mr. Potato Head-- Mr. Potato Head, being the original loot box, the original DLC for your potato. And he's 69 years older than the oldest iPhone that plays Fortnite. So a lot of the folks that are thinking about this, considering this, it's not their generation that's experiencing it and living it. And I think it's really important that we start talking about that as well. We have younger elected officials coming in, which is wonderful. But there's definitely a long way to go here.

So I think the biggest part in removing this frustration that the gaming community has with government and regulation is really changing the tone. Our leaders are often very critical, as recently as the last few days, about video games, blaming them for all sorts of social ills that studies show are just not the case.

The other part of this that I think is really concerning was just touched on by Renee, that if we regulate this too severely, so much of the game industry's profit is coming from this area, that regulations here could have a real impact on people's lives, on people's jobs. It could cause some of these companies a pretty serious amount of damage. So it needs to be taken very carefully. It is not a game. These are people's lives.

Dialogue is needed because we need to change the tone of this. When you have the President of the United States saying that games create monsters at the same time that our clients and people in the game industry are raising millions of dollars to cure cancer, it just strikes a deaf ear and makes people not feel very collaborative about this. And because of that stuff, I think things like this loot box workshop, panels, these kinds of discussions and dialogue are really positive and really give us a great opportunity to start looking at that game industry properly. So thank you guys for your time.

[APPLAUSE]

BRITTANY FRASSETTO: Thank you, Omeed, and thank you to all the panellists this morning. At this point, we're going to take a short 10 minute break before the moderated discussion. It is about 11:50, so if you can be back here at noon. And if you have any questions that you haven't already filled out, please fill out a comment card or tweet us @FTC hashtag #LootBoxFTC. Thanks.

[SIDE CONVERSATION]

[MUSIC PLAYING]

[SIDE CONVERSATION]

ANDREW WONE: OK. Welcome back to the moderator discussion for panel one. We've heard some interesting presentations this morning on loot boxes and the microtransaction landscape. And now we'd like to discuss some of the issues that were raised this morning in more depth and also take some of the questions that we've received from the audience.

To start off, we thought we'd start with a question pertaining to EA's announcement. And given their intent for its members to disclose odds for loot boxes, we were wondering first whether game developers or publishers used dynamic odds in their loot boxes, and if so, how those odds would be disclosed.

MIKE WARNECKE: Sure. So speaking to the commitment, the commitment would apply to whatever the particular loot box is. And regardless of the method used to reach the odds, those odds would be disclosed. What I can say on those dynamic drop rates is that there are a lot of innocuous uses for those that are perfectly legitimate, for instance, in a sports game that's mimicked on real world sports teams. You would want to have the players have continually updated stats.

And, for instance, if you have a baseball player that had a really good month of gameplay, their overall ranking is going to go up over time. And as that ranking goes up, they will move into higher levels of rarity. And so that is perfectly acceptable. In fact, if you had a sports game and you didn't continually update it to reflect that, the consumers would be upset by that experience. So that's an appropriate use of dynamic drop rates. I'm sorry. Did you have--

ANDREW WONE: I guess, given how would those odds be disclosed, does the fact that their dynamic influence how the odds are disclosed to consumers?

MIKE WARNECKE: Whatever odds are disclosed will be the current odds for that situation.

BRITTANY FRASSETTO: All right. So this question I'll initially open up to Jeff, but others can weigh in, just because, Jeff, you discussed this in terms of talking about the various types of loot boxes. So with pay-to-progress or pay-to-win, do you think that those are ever appropriate? And if so, what kind of disclosures would you like to see to properly inform consumers that they'll likely pay those costs or what is the total cost of the game going to be?

JEFF HAYNES: That gets to be a little bit complicated. Pay-to-win style games, by and of themselves, you're basically walking into a situation where you know the floor is already somewhat skewed. If somebody has more money or they are more willing to get an edge over you, they will have that edge. So by and of itself, you're walking in at a disadvantage. And that almost proliferates an arms war, where it's essentially, I'm not going to have a chance to compete unless I wind up getting certain items or certain gear or I dedicate a ton of time.

Pay-to-progress, on the other hand, gets to be a little bit trickier. I think when you get to things like-- especially if you have any parents and you've been subjected to Harry Potter Wizards Unite. I know I've gone to many a park looking for ins because my kid wants to cast spells and the spell energy just constantly runs out, so you're always running to a park.

And it becomes this whole situation where you can't really go through all the content, but it's this back and forth yo-yoing of, I only have this amount of time and either I'm going to pay money to go further or I'm going to have to wait a certain amount of time just to get a little bit further ahead in the game. And in some cases, it's useful at least in metering out what is being done.

So if the developers haven't created certain content, they can have additional time so players aren't blowing through everything that's there. And then all of a sudden, they go, I want to move to something different. But in other cases it becomes a problem because it's like, oh, pay this amount of money to get an extra advantage, pay this to replenish everything and go ahead again. And that's where you start getting a little bit of the tax that nibbles away at your bank account.

SEAN KANE: If I may add something to that. It's interesting because there's two perspectives on this, and so some of the pay-to-play or play-to-win. You've got games that are more individualized and then games that are more multiplayer. And so I know lots of people that'll play something like Candy Crush or one of the other game, where really, they're not playing against anyone but the computer and they're still deciding to pay to help solve a level or they're deciding to pay to get another life or whatever they might be buying in that particular game. So for them, it's individualized.

But then on the flip side when you have the multiplayer games, some people in the community will actually police some of these play-to-win or play-to-power-up scenarios because just because you have the ability to purchase that level 99 invulnerability doesn't mean you know how to use it in the game. And then in many cases, you have the community of that game itself self-selecting out those particular players because they feel that, yes, they might be overpowered in certain ways, but don't actually know how to play the game.

And so those overpowered things does not actually help them and makes some of the gameplay less entertaining for people. So I think it's an interesting dichotomy.

JEFF HAYNES: Yeah, that's true. Although there are also-- on the other hand of that, there are the situations where in some games you have players that will all of a sudden acquire different characters. For instance, there was a situation within Marvel Strike Force where, all of a sudden, a gamer should get a character that was basically being eked out in a drop rate of about maybe one or two shards per box.

And all of a sudden, this character had it within, say, about a month or two of the game basically being released. And everybody went, wait a second, how did you even do that? And it became a situation where you realized that character was already overpowered than virtually any other character in the game. And it was a circumstance of, well, who wants to challenge this player? Because we already know that the game's been basically broken wide open. This guy will beat you, doesn't really matter.

But then, is there even a point in challenging that? Or is it something where they're going to have to restrict how they even enter into it? And it becomes a situation where you realize, well, maybe they've got this advantage because they decided just to spend the money for it. And that becomes

one where, true, the community will police it, but it also becomes a situation of, do we enter this arms race or do we just abandon it altogether?

MIKE WARNECKE: Something I'd like to add to that, too, is that when situations like that arise, game publishers are very good about monitoring the in-game world to make sure that there's balance and our constantly making corrections to ensure that the other players have a good experience.

JOHN BREYAULT: And just to add one more point just to underline thing Omeed said during his presentation about the impact that multiplayer and being part of a clan, for example, can have in someone's willingness to spend money. I think it's important for the FTC as it looks into this issue further to examine their-- I know in games that I play, there's a lot of pings and nudges to join a clan or to add my Facebook friends or to create basically a social group within the game to the extent to which the creation of those social groups and the influences to join clans may be affecting someone's willingness to spend additional money on the game or not.

I think it's one issue that, I think, Omeed raised that it's important for the FTC to look at as well.

BRITTANY FRASSETTO: OK. And just as a follow up on that in terms of the disclosures at the outset-- and this is open to anyone-- I guess, how would you recommend in a game where it is pay-to-win you disclose that upfront? Is it enough to just say, in-game purchases as it is now? Or should there be more of a specific, here's what it costs for xyz purchase?

JOHN BREYAULT: So I would say that the current-- while I appreciate the efforts that ESRB has done to try and make disclosures better, I don't think that simply saying on a box that you have any in-app purchases available adequately informs your typical parent or consumer just about the level of investment that goes into trying to get people to spend more on a game or in the app.

So I don't think that necessarily just saying that up front is sufficient. Some ideas that I've seen floating around there which I think are worth exploration are disclosing what is the average spend on this game by people after they acquire it. I think that might be useful in helping consumers understand, OK, chances are that I'm probably going to spend \$10 on this game over the life of the game, or to be really good and be in the top 1%, we're spending thousands of dollars on this game.

I think that would be useful information in the hands of consumers to help them make a more informed decision.

MIKE WARNECKE: Something I'd like to add to that. From a parent's perspective, one way that may be simpler, instead of going game by game as to what the anticipated post-purchase expenditure might be, is to just set the spending limit in the parental controls that would apply across all games. It's just more efficient to do it that way.

JOHN BREYAULT: And there's no reason you couldn't do both.

JEFF HAYNES: Yeah, I actually would think that, in some cases-- just to build off of something that John said, I think. Having the label that simply says in-app purchases or in-game purchases doesn't fully explain what those purchases happen to be. And so it might be actually worth it to have a web page that actually lists whatever the content might be that parents or consumers could go to to actively see what the content would happen to be, especially in some cases for, say, sports titles, which are constantly updating with content or situations based off of real game scenarios, so that players can test their own skills against what happened in a game.

So it might be a situation where it's like score 50 points. Can you score it faster? Can you score it with these players? And at least you have more of a sense of what the in-app purchase or the in-game purchase happens to be, so you always have a sense of how the costs will change. Because setting a limit is fine, but if you realize all of a sudden you need to spend extra to maybe get a certain scenario or get a certain purchase, that spending limit will quickly evaporate, especially if you wind up always paying for a new pack, a new player, a new stadium, something else.

SEAN KANE: Well, I think we're looking at a couple different issues here. Because we're talking about certain things about disclosure and whether or not-- as John said, what's the average player spend. Well, so the real question on that has been, what's the average player? Is that a player that spends or doesn't spend? Because that could really change your numbers right there. But secondarily, Jeff, you're talking more about children or parents and them understanding more. Some of the games that we're talking about here are not games for children.

JEFF HAYNES: Sure.

SEAN KANE: Some of these games, basically-- we obviously have COPPA that Renee mentioned earlier. Most of the companies here, if they have knowledge that a child is 12 years old or younger and has an account, that game will shut down that account because that particular age is not necessarily welcome within that game. And there are other games we're talking about that are rated by the ESRB as older, mature, that sort of thing. I know kids that play those games.

Now, part of this goes back to the parents. Parents need to have an active role in deciding what their children are going to do if we're talking about children. But it seems like we're talking about all of these different issues right now, and everyone's trying to lump them together into one thing and in certain ways, vilifying these mechanics which are geared towards different types of players in different types of games in different types of scenarios. And I think we need to be really, really clear what point we're addressing to what subgroup within that.

JEFF HAYNES: I absolutely agree with you. But I think in some cases, just to counter that, there are absolutely certain games-- for instance, to use the MLB, The Show reference, there are plenty of kids that will play MLB, The Show. It's not to say that that game is for mature audiences. It's a baseball game, and so there are going to be plenty of kids that want to get their favorite players, they want to get their favorite packs. Just like with FIFA, you have plenty of players around the world that want to get their favorite football players.

And in many ways, even though there are the COPPA regulations that basically say you can't have it if you're this age with this account, it's very, very difficult to also then take somebody and

say, but now you need to understand all of the varying little idiosyncrasies when it comes to every single pack. Which is why I was saying having an extra page that maybe explains what some of the additional costs might be or what some of the extra packs are also protects some of the developers because at least they could say, we listed that there are in-app purchases, here's where you can find them.

But then for parents-- because parents do need to have role in this so that it's not simply a situation where they establish an account, they pay absolutely no attention, then all of a sudden they go, how did I get \$1,000 worth of charges? At least that way they know if my kid is playing baseball, I know that they're playing baseball. It's a safe game, but then I also know exactly what the charge might be if they want to try and find their best players for their particular team.

SEAN KANE: Yeah. And again, I think the disclosure is wonderful, I think what the ESA is announcing is wonderful. But I always go back to the point where an online shop, like Amazon, or a brick and mortar, like Macy's-- I've known people that were compulsive shoppers and they will go out and they will spend their rent money on whatever item they feel like they need to have.

Personally, I just don't feel like it's Amazon's or Macy's roll to have to step in and be the parental figure and tell these people, you can't buy this. And I think sometimes that's the economy we're dealing with, is that pressure is being put on an industry to take on a role that may not be something they need to take on.

Disclosure is wonderful and I think we all need to understand what it is that we're buying. But it's a matter of how you do that. It's a matter of how clear it is and whether or not we're being clear to the industry as a whole across the board or if we're trying to create clarity for one particular outlying individual. And I think we can't do the latter.

All we can do is basically put out disclosure that in as clear sense as possible makes people understand what they're getting, what they're purchasing. And if they decide to do it because they love that game, then that's their right to do it. I don't think that we as an industry needs to step into that parental role, though. Because some of these people are not children. Some of these people are our age and they're spending \$1,000 on a game that they love and this is their way of relaxing after a hard day's work.

JEFF HAYNES: Absolutely, I completely agree.

ANDREW WONE: OK. We'd like to turn to ask one of the questions we received from the audience, and this is a question that they're directed to ESA. "Will the newly announced standards or policies develop active strategies that parents can use to talk with, educate, or monitor their children? Will it include resource referrals to Gamblers Anonymous or other similar public health organizations?"

MIKE WARNECKE: So separate and apart from the announcement on the drop rates disclosure, as will be discussed later this afternoon, ESRB will be announcing some greater educational

efforts to reach out to parents and inform them about parental control features, including spending limits. In terms of your question about-- what was it, Gamblers Anonymous?

ANDREW WONE: Yes, that's what the one person--

MIKE WARNECKE: So, no, it does not include any sort of hotline for that. ESA's position is that loot boxes are not a form of gambling and that it wouldn't be an appropriate solution to that issue.

BRITTANY FRASSETTO: All right. The next question is for Omeed, but, again, anyone can jump in. Someone had talked earlier about online content creators and are they properly disclosing their relationships to the companies. So curious based on your expertise, "do video games pay these content creators to open loot boxes? Do they pay for the loot boxes? And if so, do they, at times, give them better odds than the public at large? And how much of that is disclosed?"

OMEED DARIANI: Yeah, that's a good question. So, yes, companies do pay for that sort of thing. It's pretty uncommon for it to specifically be, hey, just open a bunch of loot boxes. But we've definitely seen that. It happens more in the eSports type games. I've definitely been in a room where a publisher said we could do better odds on the packs that this person opens for promotional purposes. That's only been one time.

But, yeah, I think in general, content creators very often open the loot boxes because audiences really enjoy that. It's exciting. You don't know what's going to come out. You don't know if they're going to get the rare stuff. And, hey, I don't have thousands of dollars to spend on buying my own loot boxes, so I can watch someone else do it and live vicariously through them.

BRITTANY FRASSETTO: And to the disclosure point, I guess, how do content creators go about disclosing all of the various aspects that they're paid at all, that they're paid for the loot boxes, they're getting better odds, things like that?

OMEED DARIANI: Well, so I've never heard anyone disclose that they're getting better odds. So, in general, content creators are supposed to abide by the FTC endorsement guidelines. For our clients, we are very strict about that. We provide-- obviously, it's in the contracts, it's in the agreements, it's also in their notes for the activation itself. So you have a tweet, hey, a reminder to put hashtag ad or mention that it's sponsored, things like that. Very important to us because we want to make sure that we're staying on the right side of this.

That sad, content creators are sort of mixed in compliance here. We see a lot of cases where things are not disclosed properly or disclosed at all. So it's certainly an area where there could be some improvement. But from our perspective, it's a matter of education. What's really interesting about it to me is that content creators are actually, much more so than traditional celebrities or actors or things like that, they're not ashamed to admit that they're being paid for these things.

In fact, it's actually a benefit to them in a lot of cases. Because it's like, look, EA is recognizing that my content has value. They're paying me, they're supporting my channel. Because of the

work that we've done, the community that we've grown together with our audience, these big companies are involved now. And that, for many people, can be a source of validation, a source of growth, a badge of honor, that sort of thing.

SEAN KANE: If I may on that. So we've actually handled several FTC investigations into influencers in this space. And I will say that-- so I've had a lot of experience with the endorsement guidelines. One of the things I will say, a question I get quite a lot, though, is, what really is the required disclosure? And how do you go doing it properly? And that's sometimes a problem, I think, for certain content creators.

They don't know whether hashtag Spawn or hashtag ad is sufficient or it needs to be more. And does that need to be stated on the screen when they're talking about a particular game? And when? Because some of these streams are an hour long or multi-hours long. At the beginning of that stream, someone might say, I've been compensated by EA for the play that I'm doing today. Or, I've gotten this game for free to play this game today.

OMEED DARIANI: Yeah, and to build on that, not only a course of several hours, but a course of days, weeks, months, years.

SEAN KANE: Exactly.

OMEED DARIANI: So if EA gives me a copy of Battlefield 9 and I disclose, like, hey, thanks, EA, for giving me this copy. I have to disclose it every time I play the game--

SEAN KANE: But do you have to disclose it every five minutes in a three-hour stream? What happens if I come in 10 minutes in and I didn't see the beginning?

OMEED DARIANI: Yeah, we had this conversation with a lawyer at the FTC. It was more of an educational, fact finding thing. But he asked the question, which was very good, it's like, how do I ensure that everyone who watches this Twitch channel fully understands? And the answer that I had to give him was, it's impossible. You would literally have to have a platform level solution that is blocking every person coming in, like an age gate, and telling them that this is happening, in addition to having the person talk about it constantly.

Because unlike a recorded video, people come in and out. So it's not like if I watched the first 30 seconds, and then five minutes, and then five minutes, I'm going to see one of them. I could just be there for a time where there's no disclosure.

SEAN KANE: And right now, the influencer can't-- like, Ninja, if he wanted to, couldn't be like, I'm going to put this bar that pops up on Mixer that now says, I'm getting compensated for this. Because I don't have control over that platform or the distribution method.

OMEED DARIANI: Yeah. And even when Twitch does sponsored streams, sometimes, not always, but they'll require that there's an actual badge on the screen, like, sponsored by EA or whatever. But that's not always required and that's certainly not a platform level solution. They send the image to the broadcaster and the broadcaster puts it into their broadcast.

ANDREW WONE: OK. We're almost out of time. It's just a final wrap up question to all the panellists. "What direction do you see the industry moving towards in the future relating to loot boxes and other in-game purchases? And will freemium games with microtransactions continue to be a popular model?" Whoever would like to go first.

JOHN BREYAULT: From my point of view, I don't see any reason why the industry would turn away from a game model that is becoming increasingly profitable for them. In terms of the disclosure, just to underline what other folks have said, Michael's announcement on ESA loot box drop rates is important, and I think it does show that this is an industry, unlike other industries, where you often see people like me criticizing. It's one that does seem to pay attention to its users and react fairly quickly to them. And so for that, I think they should be applauded.

But at the same time, I think it's important for the FTC to maintain a close eye on this. This is an industry where, as have been said many times, hundreds of millions of people are playing them and it's generating billions of dollars in revenue. And so to ensure that the industry doesn't take advantage of gamers in its efforts to continue that profitability is an appropriate role for the FTC to take.

RENEE GITTINS: I think that the freemium model is a core part of the app economy, not just within games. We see it in fitness apps and other apps as well. And I think consumers are getting really used to that. It's risk-free for them because they can try out any applications prior to purchase. And when consumers are introduced to games on this freemium model, I believe that they begin to expect that on consoles and the PC market as well. So I think we'll continue to see growth in that area.

OMEED DARIANI: Can you imagine if the freemium game model existed in that time period where AOL was just mailing CDs to everyone every day? World of Warcraft doesn't make most of its money from the \$49.99 box. It makes most of its money from \$15 a month. You could very easily see a situation where they're just sending those disks to everyone and is like, hey, just try this for a month and see what you think. But I think download speeds caught up, so that was never necessary.

But can you imagine going back to the '80s and telling little Omeed, this game that you're playing could just be free-- like, it's just free. It's like, oh, my god, how did that even happen? So it's pretty amazing that this business model exists.

SEAN KANE: I think the industry is going to continue to strive to provide better and bigger experiences to the users and do it in a way that tries to be at a price point that makes the most sense. And I think there's going to be ebbs and flows, there's going to be a success and failures because different methods of monetization are going to work for the industry, but maybe not work for the community. And so there's going to be a learning by both sides.

And as technology increases and changes, we're going to be seeing things differently. So personally, I think that all of these issues makes it certain that my grandkids are going to be around still questioning what's new and what's going to happen. It's going to be a great ride, I think, for all of us to see where we're going to go.

JEFF HAYNES: Yeah, I think it's going to be really interesting, especially since we're on the cusp of a new generation of hardware coming out next year. And I think that there are certain models that work really well. I think sports games really have a pretty good grasp of the loot box mechanic when it comes to certain content. But I think the game industry, in some quarters, are moving away from it.

At E3, there were a number of companies that said no loot boxes, no microtransactions in this game ever, and it was this huge flag that they were planting down. And it was one of those circumstances where, I think, some game types or some games genres, that mechanic hasn't worked very well. In others, it works perfectly. And I think sports, especially with it being such a dynamic situation and developers trying to capture that dynamism in game as realistically as possible, it winds up providing that perfect marriage of the two.

On the other hand, when it comes to mobile apps, I think there's going to be a larger explosion of that, with possibly the exception of whatever the Google Pass or the Apple Arcade announcements will be and how that will be handled. Because if it winds up being a situation where you pay in for a subscription to have a certain kind of experience without ads or without in-app purchases, that could radically change the landscape of how apps are even being handled and measured with loot boxes or microtransactions going forward.

MIKE WARNECKE: Few industries innovate as quickly and as frequently as the video game industry. And we're constantly experimenting with new ways of reaching consumers, new ways of providing them a range of experiences. And as Sean mentioned, and I agree, sometimes we get that right, sometimes we need to make adjustments. And I think that that's always going to be the case. And I think consumers want us to continue to push to see what new experiences we can offer and what new ways they can enjoy gameplay.

And so I can't say where the direction of the industry is going to go in five or 10 years, but what I can say is this. It is a customer-focused industry. And when gamers are upset or have concerns about a particular implementation, there is an incredible feedback loop to the publisher and to the industry about what works, what doesn't work, what can be improved. And so I imagine, regardless of what the technical platform will be for the future, that feedback will continue and the industry will continue to be responsive to the gamers who help support us. Thank you.

BRITTANY FRASSETTO: All right. Thanks, everyone. And thanks to the audience for a good morning panel. All right. So we're running a little bit late. I see it's about 12:30, so we still want to give you guys about an hour for lunch. So if we can reconvene for panel two at 1:30, that would be great. Thank you.

SEAN KANE: Thank you.

[APPLAUSE]

[MUSIC PLAYING]