



A Letter from the Chairman

Dear Colleague:


According to a recent article in the *New Yorker*, “Independent, publicly traded American newspapers have lost forty-two percent of their market value in the past three years.” The McClatchy Corporation, a very large newspaper publishing company, has lost more than eighty percent of its value since purchasing the Knight Ridder chain in 2005, the magazine reports. Even the market cap of the venerable New York Times Company has declined in value by more than fifty percent in the last three years.

Clearly, the economics of the media industry are changing dramatically. Few consumers under the age of 30 consider print media their principal source of news and information; indeed, few even read newspapers with any regularity. With increasing frequency they are turning to digital and electronic sources of information, which offer immediately updatable content as well as the ability to offer other types of services and entertainment that print media cannot even contemplate.

What are the consequences of this to us, the media liability insurance community? Are we adjusting our product offerings and underwriting capabilities in step with these rapid developments in the industries we serve? If one scans the media liability insurance landscape, the answer is, “Probably not.” In the last few years, several new insurers have entered the traditional media liability insurance marketplace in the U.S., serving the print and broadcast industries – notwithstanding the fact that it is probably no more than a \$200-\$300 million dollar marketplace, and shrinking fast if the *New Yorker* article and other similar sources are correct. For the most part – and we at Media/Pro are occasionally as guilty of this as others – media liability underwriters continue to offer the same types of products and continue to view “media liability” coverage in isolation from other emerging coverages, particularly technology-related exposures.

In this publication, we regularly explore these themes and their consequences on the industry segments that we serve. In this issue, for example, we explore in detail the phenomenon of virtual worlds such as “Second Life” and related websites, and the corresponding new exposures and underwriting challenges that they create. I confess that I was initially skeptical of the relevance of this topic; but I think that, after reading this issue, you will agree that the implications of this new technology are mind-boggling. We look forward to working together with you over the coming years to develop insurance solutions to these challenges, as we all work toward developing our “second life” as insurance professionals in the digital age.

Sincerely,

 Leib Dodell
Chairman
Media/Professional Insurance

The Commercial Marketplace in a Virtual World

By Barb Wood
and Chanda Feldkamp

Searching for new and innovative ways to market their products and services, many companies are tapping into the virtual world market. Far from the first commercials seen on black and white televisions, this new marketing venue requires an extensive imagination. Companies such as Coca-Cola, Motorola and Wells Fargo have opened virtual stores in these virtual worlds, or have created their own virtual world to promote and sell their products.

The question for insurance professionals is: will these companies' activities in virtual worlds create professional liability exposures for them as real world service providers? After examining the seemingly endless scope of virtual worlds, it is clear that exposures are real even if not entirely known.

While virtual worlds seem far-fetched to some, there is a vast amount of real money being exchanged. Participants in the virtual world Second Life spend \$30 million in U.S. dollars per month for digital goods and services. For \$3.00, you can buy a yacht. A musical instrument, that you can actually play, costs \$10.00. A castle will set you back \$55.00, while your own island can cost you \$295.00.

To capitalize on the consumer interest, there are varying ways in which companies can become involved in virtual worlds. For commercial enterprises seeking to establish a virtual world presence, however, the costs can be steep. One marketing firm has recommended to some clients that they should allocate up to \$1 million to create a virtual world experience.¹

Some companies have retained information technology consultants and marketing firms to create and manage their virtual world presence. These vendors' miscellaneous errors and omissions exposures are very similar to the exposures they have working with any other client.

Global retail companies have also opened virtual world stores that not only sell virtual versions of their products, but also link to the companies' real world web site for purchase of the real world product. For these real world companies who have created virtual world counterparts to sell their real world products and services, there are concerns that go beyond simple advertising exposure.


For instance, in an attempt to capture the attention of the online community, Sears opened a 3-D showroom on an IBM "island" in the virtual world of Second Life.² This "store allows consumers to experiment with changing the color of the cabinets and countertops in a virtual kitchen, explore 3-D versions of various home theater set-ups and learn how to organize their garage by virtually customizing storage accessories."³ Consumers can then order items chosen in the virtual Sears showroom for their real world home, "by connecting from the 3-D environment to Sears.com and choosing delivery to their homes

or the option to pick up the items in their local Sears store."⁴ Just as with other e-commerce transactions, these transactions create unauthorized access exposures, intellectual property infringement exposures, and exposures to regulatory actions.

Taking it one step further, some real world companies are strictly selling virtual world products and services, but for real U.S. dollars. There are virtual world real estate firms selling virtual properties, virtual world employment agencies steering avatars to dream jobs, and virtual world interior designers helping decorate virtual world mansions. The setting is virtual, but the money and the potential for real world liability exposure are real.

Where there is the potential for a financial loss, there is the potential for a professional liability claim. Recognizing the potential exposures, online auction house e-Bay decided to "ban auctions for the characters, currency, weapons, attire and accounts" of certain virtual world games.⁵ An e-Bay spokesman indicated that the decision to pull these items was due to the "legal complexities" surrounding virtual property.⁶

Only time will tell how these virtual world exposures will impact the legal and insurance industry. However, it is evident that it is not a fad, and companies seeking to establish a virtual world presence will need to consider each risk carefully and consider the potential exposures that each virtual world participant may encounter.

 Barb Wood is an Underwriter at Media/Professional Insurance, and Chanda Feldkamp is a claims counsel at Media/Professional Insurance.

¹ Joyce Schwartz, *Bold New Opportunities in Virtual Worlds*, (March 10, 2006), <http://www.imediainconnection.com/content/8605.asp>, quoting Erik Hauser, founder of Swivel Media.

² IBM Press room, *Prototype "Sears Virtual Home" to Open on IBM Island in Second Life*, (January 8, 2007), <http://www-03.ibm.com/press/us/en/pressrelease/20862.wss>

³ *Id.*

⁴ *Id.*

⁵ Daniel Terdiman, *eBay bans auctions of virtual goods*, (January 29, 2007), www.news.com/eBay-bans-auctions-of-virtual-goods/2100-1043_3-6154372.html

⁶ Slashdot.org, *eBay Delisting All Auctions for Virtual Property*, (January 26, 2007), <http://games.slashdot.org/article.pl?sid=07/01/26/2026257>

A Virtual Twist on Traditional Perils

By Russell Hickey

“Buy land, they’re not making it anymore.”
- Mark Twain

Since the advent of the Internet, conventional wisdom has been changed in many ways. With the rising popularity of online virtual worlds, even Mark Twain’s seemingly sage advice has been proven wrong — new land is being created every day in virtual worlds such as Second Life.

In virtual worlds, newly created land has begun commerce. In November 2006, Anshe Chung became the first Second Life real estate tycoon to earn more than \$1 million by buying and selling virtual land.

With commerce comes news — and a Second Life presence of the international news service, Reuters. There is also the Second Life News Network, which offers “in-depth reporting on news and events in Second Life and Real Life developments that affect Second Life.”

But does publishing in Second Life and other virtual worlds come with standard media perils? If so, are current laws sufficient to handle the virtual-world media perils?

For any company considering a presence in a virtual world, it’s important to carefully review the activities planned for the virtual world presence and consider the potential exposure created by dealing with and writing about virtual “people.”

In Real Life, the U.S. laws on defamation have been relatively established since the 1960s. Many basic questions, however, are being asked anew thanks to virtual worlds. Last summer the *Brooklyn Law Review* published an article questioning whether current laws are sufficient to handle defamation claims arising in Second Life.

Take, for example, a standard news story about a criminal suspect charged

with assault. In Real Life, presumably, much of the story would be based upon police reports and other official governmental records. Other sources could include interviews with the victim, the prosecuting attorney, and the defense attorney.

In a virtual world, however, a standard news story, with standard sources and standard Constitutional protections, becomes anything but standard — beginning with the alleged crime.

In reporting on the crime, a host of questions immediately come to mind. First, and most basic, could a story about an avatar’s crime potentially defame the avatar’s owner? Has the avatar’s owner committed any wrongdoing?

Other basic assumptions about a standard news story seemingly disappear in the context of a virtual world. While Second Life owner, Linden Labs, acts in a role akin to the police and/or prosecutor’s office — they are by no means a governmental agency, and thus carry no privileges upon which a media outlet could rely.

These questions simply scratch the surface of the potential questions a Real Life court could be asked to answer when hearing a Second Life defamation lawsuit.

Defamation, however, is not the only standard media peril Real Life companies potentially face in the virtual world. A quick scan of the types of organizations now existing in Second Life, and other virtual worlds, gives a good indication of the questions important to users.

In January, the Virtual Intellectual Property Organization opened in Second Life. According to its website, the VIPO offers “expert legal advice on trade and

commercial issues in virtual worlds as well as intellectual and virtual property matters.”


The lesson? Protecting intellectual property is a hot-button issue in virtual worlds.

Last fall, six major content creators filed a lawsuit in the United States District Court for the Eastern District of New York alleging a Second Life user had wrongfully duplicated thousands of products sold by the content creators. They alleged copyright and trademark infringement.

One of the six content creators, Eros, had previously filed suit in the United States District Court for the Middle District of Florida. Eros also alleged copyright infringement based on the unauthorized copying and distribution of one of its most popular products, the SexGen bed. This suit was the first Real Life suit alleging copyright infringement in Second Life.

Surely, as much as protecting one’s own intellectual property will be important, ensuring against the unauthorized use of another’s intellectual property is equally important — including the ever-developing rights of publicity. It seems only a matter of time before a celebrity will sue a virtual world company for staffing its presence with avatars resembling a Real Life celebrity.

In a run-up to a virtual world presence, it will be crucial for companies, media and otherwise, to understand the landscape of virtual worlds prior to diving into the flow of virtual world commerce. In a virtual world, standard risks may no longer be so standard — and that may translate into real-world exposures.

 Russell Hickey is a Claims Counsel at Media/Professional Insurance.

Partnering For Success In A Virtual World

By Jon Van Meter

As activity in the virtual worlds increase, the insurance industry is under pressure to respond to the need for coverage. We asked a few of our technology brokers to elaborate on their experiences with virtual worlds and to look into their crystal ball for where the industry is heading.

**Becky Pearson, Carpenter Moore,
San Francisco**

There are a variety of virtual environments on the Internet, and the scope of user interaction generally will define the types of risks that the provider and virtual inhabitants face. Some providers encourage user participation by recognizing intellectual property rights within the virtual world. In turn, those inhabitants have used these intellectual property rights to earn virtual dollars, and in some instances translated that virtual currency to real dollars. Because of the potential money-making aspects of these rights, there are already reports of inhabitants trying to enforce their rights by suing other users for infringement of their copyrighted content in the virtual space. Consider the other transactions that users complete in the virtual world — purchasing virtual property, buying goods or services, participating in currency exchange — and one can anticipate an explosion of disputes among users and with the provider.

Given that many providers try to avoid involvement in these types of disputes, users are resorting to resolution outside of the virtual world. The problem, however, is that the assistance of the provider is needed to identify real people. The provider's own privacy policies may prohibit or at least require certain legal processes to release that information. At the end of the day, a user may find it too difficult to pursue that information, and simply turn to the provider to obtain the relief they are seeking.

At present, while considering these issues, the most viable insurance risk probably lies with the provider. The extent of the issues and disputes caused by participating in the virtual world, however, have not been fully developed. It's likely we've only seen the tip of the iceberg with respect to claims and the likely targets. Although disputes may currently be focused on ownership rights, they could easily expand into other real world problems, like theft, fraud, stalking, and even identity theft. Further, if these worlds continue expanding in the future, it is likely that the commerce and business aspects will dramatically increase, as well.

As the virtual issues spill over into the real world, providers will probably need to establish a dispute resolution process to maintain order in the virtual world. At that point, it is likely that we will see insurance becoming a more viable option to address these risks, not only for providers, but for the users.

Steve Haase, InsureTrust, Atlanta

The advertising/marketing folks can't resist exploring the possibility of deriving new revenue and customer loyalty with these new solutions.

In addition to privacy, security and identity theft concerns, there is the very real possibility of cyber stalking. The statistics are overwhelming that predators have found new confidence through utilizing the web to approach potential victims. Contingent bodily injury type coverages are becoming popular.

The return on investment from including virtual worlds in an overall marketing/advertising plan are potentially tremendous. The result is that companies will be compelled to experiment with these in order to remain competitive. Risk managers will have to revise their insurance programs to contemplate these emerging risks.

**Alex Slawson, Tri-City Insurance,
San Francisco**

Virtual worlds that provide more functionality, including Second Life, but also many massively multiplayer online games, often provide both more immersive environments with more realistic avatars, and more tools to allow users to interact with and alter their environment.

These two factors — an immersive environment and high functionality (the ability to create, customize, alter, share, trade, sell, etc.) — create an ideal environment for third-parties to find related business opportunities within the virtual community.

We recommend that clients purchase a broad policy that provides the four main aspects of Cyberliability: E&O, Intellectual Property Infringement, Media Liability, and Security & Privacy Liability.

Our virtual community clients usually seek coverage primarily to address their media liability exposure. We find that many underwriters are reluctant to provide media coverage for virtual communities because, as with more traditional social networks, the

behavior of a virtual community's constituents is inherently unpredictable.

We also recommend that our clients' technology policies include contingent Bodily Injury & Property Damage to the extent that this coverage can be obtained. As with any medium that allows for social interaction, there is always a possibility that one member of a virtual community may cause physical harm and/or emotional distress to another member.


Virtual communities also pose a distinct network security and liability exposure, and the network security scenarios that could result in liability to the community's operator are myriad. Many virtual communities rely and thrive upon their members' anonymity, and a security breach that results in the disclosure of such members' identities would likely result in multiple claims. Massively multiplayer online games are also susceptible to various security breaches including but not limited to denial-of-service attacks and theft of player accounts.

More often than not, our virtual world clients are compelled to purchase cyberliability coverage by their general liability carriers. CGL policies provide several types of real-world coverage, including Personal & Advertising Injury, Bodily Injury & Property Damage, that are not intended to apply to virtual world exposures.

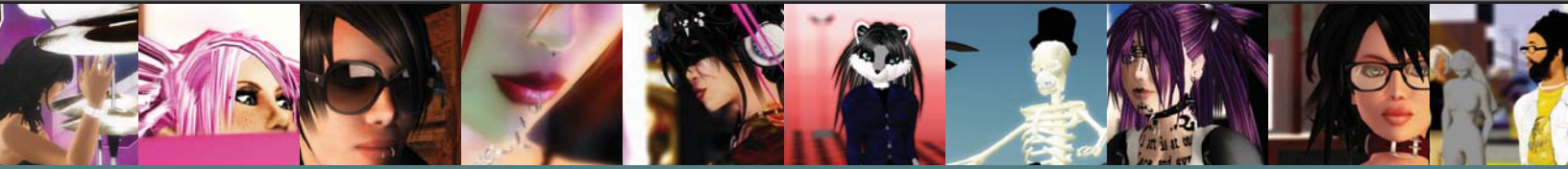
Ultimately, I can see two long-term outcomes, the first of which is that legal developments afford underwriters a better sense of the extent of a virtual world's vicarious liability. Several legal issues remain unsettled, including question of ownership of virtual property created by users.

The second long-term outcome would entail that increasing claim frequency and severity results in a constricted or fractured insurance marketplace, where only a very few insurers are willing to participate and then only for certain specified perils.

There may remain certain sites that, by virtue of the scope of their operations, remain uninsurable. For the majority of virtual worlds, however, open communication and cooperation between clients and insurers will usually engender trust, and result in success.

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Feedback or story ideas? Please send to mpisource@mediaprof.com.



My So-Called 'Second Life'®

Continued from front page

Somewhere between real life and a video game exists the virtual world, where users create avatars and, in many very real ways, live an alternate existence in this incredibly profitable enterprise. By some estimates, the collective gross domestic product of virtual worlds ranks between Russia and Bulgaria — 77th in the world.

Millions of people from around the world socialize, explore, buy and sell every day in virtual worlds. In the virtual worlds, however, there are no laws and regulations — just a user agreement for people to follow.

Virtual worlds are a binary-based space where human players find entertainment or commercial value through their avatars.

In some ways, virtual worlds are similar to traditional video games. They can offer game characters, levels, goals, economies, competition and entertainment value.

In other ways, however, virtual worlds are unlike any video game. Virtual worlds have no pre-scripted story line or purpose. Virtual worlds do not pause or start over when a player quits playing. Players freely interact and socialize with one another in venues within games, such as conference halls, casinos, cafés, movie theatres, hotels, homes, or malls.

Many virtual world users have explored their own emotional and psychological ranges by experimenting with the many different roles a virtual world offers (including gender identities). Many virtual world participants report that they have strong emotional

ties to avatars. Reports estimate 8.7% of male participants and 23.2% of female participants have had an online wedding.

Virtual worlds are also constantly growing and changing. Users create content with which they navigate, explore, and interact. This never ending environment sometimes forces players to change their real-world schedules in order to "keep up" within the virtual world.

Linden Lab's Second Life, the most popular virtual world, made its debut in 2003. In Second Life, intellectual property rights are given for participants' creations. Users are allowed to endlessly customize avatars and start businesses on the virtual land they have purchased.

In Second Life, daily trade is in excess of \$1 Million. Users can buy and sell one another's creations by using virtual currency, which is converted with real money. Participants can use a credit card or PayPal to buy and sell currency through the currency exchange.

Game publishers usually prohibit the exchange of real-world money for virtual goods. However, a number of virtual world products are used to actively promote the idea of linking to (and directly profiting from) real-world commerce.


Second Life's thriving economy has encouraged corporate America to get "virtual." Toyota Motor Corp sells digital Scion cars. IBM opened a meeting space on 12 new virtual islands for IBM employees.

Copying and other misappropriation of brand names and designs is ubiquitous in the virtual worlds. By mirroring real life, in virtual world, avatars own what humans own in real life — Nike shoes, Prada bags and Ferraris. Not all goods, though, are authentic and many infringe upon real-world copyrights and trademarks.

Virtual world malfeasance, however, is not limited to intellectual property infringements. "Griefer" is a term coined for an avatar who assaults another. In other words, "griefing" means to scam, cheat, abuse, or steal.

Due to the increasing number of legal issues in the virtual worlds, some attorneys have set up virtual-world offices where avatar attorneys provide legal advice. A group of real-world attorneys have formed a Second Life Bar Association. Second Life, like most virtual worlds, relies upon terms of service and user agreements (entered into when joining the community) to resolve disputes. There has been an increasing interest, however, in developing an online dispute resolution process.

Virtual worlds may be hard for some to conceptualize, but they are very real for their participants. Increasingly, virtual worlds are facing real-world problems which will inevitably require real-world solutions.

 Yujin Tan is an Underwriter at Media/Professional Insurance



What the...? Second Life® Jargon

Avacar

A vehicle used by a user to move their avatar some distance in the world. Also related to teleport and portal.

Avatar

Your virtual you — the digital body that you create and refine for yourself, and how others will see you within Second Life.

Griever

A term coined for an avatar who assaults another. In other words, “griefing” means to scam, cheat, abuse, or steal.

IM

Acronym for ‘Instant Message.’ Second Life’s IM service is how you chat with other people in-world.

In-world

In the virtual world of Second Life or being logged into the game.

Lag

When your avatar (or the surrounding scenery) moves slowly or jerkily due to inadequate Internet bandwidth (speed) or processing capacity within your computer.

Linden Dollars

The official online currency in Second Life. You can earn and spend Linden Dollars in-world, or you can exchange them with US Dollars via your registered credit card account.

Linden Lab, Inc.

Linden Laboratory is the company behind Second Life. They administer and host this virtual world in the real world, so they look after the computer servers, member data, member behaviour and so on.

Rez

Short for ‘resolve,’ and used like the word ‘appear.’ So your avatar can rez (appear) in-world; scenery can rez poorly (appear slowly, move jerkily, have limited depth); or items can rez badly (appear badly constructed, or move badly).



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