

Do you know your NFTs ?

What are NFTs ?

Non-fungible tokens (NFTs) are generally understood to be unique digital certificates registered in a blockchain that record the ownership of an asset such as an artwork or a collectible. Unlike cryptocurrencies such as Bitcoin, which are “fungible” (meaning one Bitcoin is the same as any other Bitcoin), NFTs are unique and non-fungible – each NFT is different from each other NFT.

The blockchain technology involved with NFTs uses cryptographic hashes and character strings so that each NFT and the transactions associated are indelibly associated with the previous elements of the blockchain and transaction data. In essence, NFTs are constituted by rights that one owns, where the details of those rights and chain of ownership are held on a decentralised register, rather than by a central authority such as an intellectual property office or land registry.

What exactly are you buying when you purchase an NFT?

NFTs don't all represent the same rights and – unless stated otherwise – the purchase of an NFT does not include the purchase of any underlying asset or any intellectual property (IP) rights – you get solely what you see, which may be only a copy of a picture.

However, when prices are able to reach the dizzying heights of \$69.3 million for the associated NFTs of digital artworks such as 'Everydays: The First 5000 Days' by Mike Winkelmann, it is perhaps understandable that the term NFT is often incorrectly used in reference to the asset itself rather than the somewhat less exciting “right to show a photograph of the asset in the metaverse”. Indeed, there is often confusion over what it is that is actually acquired. As was demonstrated in the sale of Everydays: the First 5000 Days, it is often not a transfer of the copyright. As Winkelmann told CNBC, “I think that people don't understand that when you buy, you have the token. You can display the token and show you own the token, but, you don't own the copyright”. In other words, you're buying the

token not the art itself. One might say perhaps the whole thing was more a conceptual art project than a traditional art auction.

The issue of the lack of automatic grant of IP rights was brought to light when the co-founder of Twitter, Jack Dorsey, sold his first-ever tweet as an NFT for \$2.9 million on the Valuables platform. This platform, which created (minted) the NFT, described the transaction as purchasing “an autographed certificate of the tweet”, making it clear that the copyright would not be transferred and despite the buyer, Sina Estavi, spending \$2.9 million on it, the buyer could not use the tweet itself without permission. In fact, Dorsey could even delete the tweet or make additional NFTs from it, regardless of Estavi's purchase. The lack of rights associated with the NFT didn't demoralize Estavi though, with him writing on Twitter after the 2021 auction “I think years later people will realize the true value of this tweet, like the Mona Lisa painting.” So far this doesn't seem to be the case; in April 2022 the NFT went back up for auction for \$48 million but only received 7 bids with the top bid of \$277.

Similarly, prolific Youtuber Logan Paul who invested \$623,000 in an Azuki NFT collection saw the value of the same NFTs drop to \$10 over time.

These extreme price drops are unsurprising. Hype reached a peak in 2021, and with hype drop off always comes downward price pressure. In November 2022 the NFT market was estimated to have a total market cap of \$11.3 billion (a significant drop from the high of \$23 billion in 2021) and has likely dropped further since with recent well publicised concerns surrounding “all things crypto”, and while a recent research report from brokerage and research firm Bernstein emphasised that NFTs are not dead, popular (and some may say “gold standard”) NFT collections such as the Bored Ape Yacht Club have seen prices continue to fall. With these price drops, it is not now anticipated that the NFT market will grow to \$231 billion by 2030, as some may previously have predicted.

However, NFTs remain a technically simple way to create a market in the purchase and sale of rights, whatever those rights may be. Bernstein suggests the success of future NFTs will be dependent on their ability to deliver a real product such as gaming, entertainment tickets, and content and merchandise, requiring every brand to build an NFT marketing strategy – noting the success of Nike in generating \$180 million revenue through NFTs.

How to monetise IP through NFTs

The metaverse may represent one of many avenues through which a business or individual's IP can be monetised through NFTs. It has been predicted that 25% of people will spend at least one hour in the metaverse by 2026.

The metaverse consists essentially of three-dimensional immersive virtual environments. It is predicted that it will be a place where NFTs will be commonly bought and sold in industries such as fashion, property and gaming.

Whilst there is a degree of negative press surrounding the activities of some “big tech” players in the metaverse, and the amounts they have spent with little return, it is working for some brands. Nike has developed a virtual world, Nikeland, which is free to visit but sells products and associated NFTs, to allow the use of clothing and footwear for avatars within the virtual world. One should also look at the successes of Roblox and Minecraft, and how they show virtual worlds can work. Whilst payment and monetisation mechanisms associated with such platforms remain somewhat “traditional”, it is only a short leap to visualise the integration of decentralised technologies. And the majority of users will make up a significant part of the adult population in the coming years.

NFTs can also provide a ‘real product’ outside the metaverse – for example, they can be used as a way of ticketing for in-person events. This can work solely as an access pass, including data collection/proof of attendance or even to enable deeper artist to fan interaction. For example, Coachella used various collections such as ‘The Infinity Key’ which included the benefit of a lifetime guest pass, and ‘Key to the Sahara’ which offered the perk of on-stage access in the Sahara tent during one performance in 2022.

With NFT use expanding from virtual art and avatars, the current uncertainty concerning rights and ownership is likely to grow. Although the purchaser of the NFT does not automatically own the IP rights, the seller is entitled to sell or licence the IP rights in the underlying asset to the purchaser of the NFT. This does not happen as an automatic consequence of the purchase and must be assigned in a smart contract, which

can be embedded in the NFT allowing the execution of certain actions automatically, or in a separate agreement elsewhere in express written terms. A few of the many opportunities that can develop from releasing commercial rights were demonstrated when owners of Bored Ape Yacht Club released rights to NFT holders, leading to the opening of the Bored and Hungry fast food restaurant in California, with ape-branded interior/food, and actor Seth Green planning a TV show based on the NFTs.

Within smart contracts, there is an additional opportunity to monetise IP. Automatic royalty payments to the owner of the copyright or artist (regardless of who owns the NFT) can be coded into the smart contract for each onward sale of the NFT, quite easily and simply. These royalties are usually paid as a percentage of the secondary purchase price. In contrast to the controversy surrounding music streaming failing to adequately remunerate the creators and performers of music, these royalties will ensure that the artist can capitalise from the onward sale of their work.

Copyright and trade mark issues

Minting an art based NFT can be categorised as a making a copy or derivative of an original copyright work, therefore without a licence there must be permission from the copyright holder before minting the original work into an NFT. Additionally, within copyright law there have been arguments over who owns NFT rights (much like the arguments around who owned rights to seek e-book deals in the publishing sector when digital publishing became a new option for authors). Although now settled, production company Miramax sued Quentin Tarantino for copyright infringement because he was selling NFTs associated with the 1994 film Pulp Fiction. Difficulty arose when Tarantino argued the right to mint NFTs was within his reserved rights, based on the copyright he retained in relation to the screenplay. Miramax, the owner of the movie's copyright, maintained that its copyright interest in the movie and media accounted for technology that had not yet been created in 1996 when the contract was signed. One of course may argue how there can be consensus in idem on a thing that cannot have been within the minds of the parties at the time. The case was settled before judgement with indications that both parties might collaborate in future NFTs but it nonetheless raises interesting points.

Anyone considering minting new collections should carry out proper due diligence on copyright when minting an NFT associated with an existing work, to ensure that the correct permission is obtained. Similarly, they should do the same with any relevant trade mark rights (both registered and unregistered).

An example of what can happen if you don't take due care can be seen with quick reference to Italian football. In a recent matter, Juventus Football Club discovered that the platform Blockeras had minted and advertised NFTs containing Juventus' trademarks as well as an image of former player Christian Vieri wearing his strip. They applied to obtain a preliminary injunction to stop the alleged infringing activities of Blockeras. Blockeras argued that no such injunction should be granted because Juventus' trade mark rights were limited to a different class of goods than the digital goods Blockeras made and sold. However, as Juventus engaged in business both online and physically it was found that there was a likelihood of confusion as to the NFT's commercial origin due to the fame of the team; the injunction was granted despite Blockeras obtaining the authorisation to use Vieri's image, thus highlighting the importance of proper due diligence into who the exact owner of each element of an NFT is, and obtaining proper permission.

Brand protection and enforcement of IP

There is a real risk of infringement of IP rights within the world of NFTs for any brand.

It is thus recommended that businesses enforce their IP rights by monitoring NFT marketplaces and enforcing their IP rights where there has been infringement.

Additionally, there are ample opportunities for businesses to exploit their IP through NFTs. This can be through licensing and royalties as earlier discussed, but also by using NFTs as a method of business expansion.

On top of the potential for brands to capitalise on digital clothing, there is room for creativity. Nike has secured a patent for Cryptokicks, a system that pairs NFTs to a physical shoe that will track authenticity and ownership. Whilst Cryptokicks are currently only digital, the premise of attachment to a physical product is exciting and will provide a new method to enhance the consumer experience. This technology could also be part of a brand's anti-counterfeiting strategy using a digital record on the blockchain proving authenticity. This would also prove useful for second-hand shoppers to get an accurate history of the physical product before buying as paperwork proving authenticity is often forged. This blockchain strategy was used when the rare Rolex "Paul Newman Lemon" Daytona went up for auction at Christie's which, as said by said Rémi Guillemin (Head of Watches and Wristwatches Department at Christie's Geneva) "[adds] value, both for the current owner and for the future buyer. It allows total transparency thanks to the expertise of an independent third party. This is exactly what the new generation of collectors wants".

Additional action businesses can also take to help deal with infringement include registering their trade marks in Nice Classes 9 and 35.

A brand that didn't take this step is French design house Hermès, the BIRKIN trade mark owner, whom are currently awaiting judgment on the alleged trade mark infringement of artist Mason Rothschild's creation and sale of 'MetaBirkin' NFTs. Hermès trade mark rights are limited to bags and leather goods and despite the success of Juventus, there is a subsequent trend of brands registering their goods in additional classes. Italian fashion house Gucci has now expanded its trade mark portfolio to class 9 and class 35, covering downloadable digital goods and retail store services featuring virtual goods.

Conclusions

As the use of NFTs evolves, so does the opportunity and risk for IP owners. With public uncertainty over what rights have been acquired during the sale of an NFT, emphasis should be placed by brand owners on clarifying the default IP position to avoid misuse. Brand owners should also make sure their rights portfolios are strong enough to allow brand theft prevention. On a more creative level, utilising NFTs can fight counterfeiting and provide businesses with various new methods of expanding their business. These opportunities come alongside challenges and whilst the laws of copyright and trademarks are still developing with respect to NFTs, it is a brave brand that waits to see.

Get in touch

SGBs can access the **sportscotland** legal expert resource helpline by email at sportscotlandinfo@harpermacleod.co.uk or by calling **0141 227 9333**.