Presented by THE HARVARD LAW SCHOOL ASSOCIATIONS OF SAN DIEGO, ORANGE COUNTY, LOS ANGELES, and NORTHERN CALIFORNIA and THE HLSA WOMEN'S ALLIANCE OF LOS ANGELES

Virtual Presentation
(Zoom Link to Follow Registration)

Time: 12:00 pm - 1:15 pm (PDT)
Date: Thursday, September 29, 2022

"What Every Lawyer Should Know About NFTs"

Our increasingly virtual and digital society has brought both unique opportunities and unprecedented challenges. These include new realms through which lawyers must navigate their clients in understanding, monetizing, and protecting intellectual property rights in edgy and emerging commercial marketplaces.

Squarely at this intersection are **Non-fungible Tokens** (or "**NFTs**"). Join us for a practical session led by an expert panel that will answer such questions as:

- What is an NFT? Do I need to understand blockchain and smart contracts first?
- Do only certain types of companies or products lend themselves to NFT offerings?
- What types of licenses and sales platforms are available for NFT projects?
- Does IP law impact NFT projects? What about UCC Article 2? Other laws?
- What are lessons from major NFT disputes (Nike, Yuga Labs, Miramax, MetaBerkins)?

Moderator:

Olga V. Mack, Vice President & CEO, **Parley Pro at LexisNexis** and Lecturer, **UC Berkeley School of Law** (Blockchain for Lawyers course); Author, ***Blockchain Value: Transforming Business Models, Society, and Communities*** and ***Fundamentals of Smart Contract Security***. Olga served as Quantstamp's Vice President of Strategy, the first decentralized security auditing blockchain platform. She leads Web3 conversations in her Blockchain Value LinkedIn LIVE conversations and podcast. She's held roles at Visa, ClearSlide, Zoosk, Pacific Art League, Wilson Sonsini, and Yahoo.

Panelists:

Melanie J. Howard '01, Chair, IP Protection, Loeb & Loeb (L.A.) Melanie's practice focuses on acquisition, protection, licensing, exploitation and sale of PHOTO intangible assets for major brands and individuals. A leader in her firm's Web3 practice area, she advises clients and managing deals involving blockchain, cryptocurrency, NFTs, minting, licensing and royalty structures, advertising issues and brand protection, exploitation and enforcement in the metaverse.

Mark F. Radcliffe '81, Partner, DLA Piper (Silicon Valley) and Co-Chair, Blockchain and Digital Asset Practice Group. Mark has 30 years of Silicon Valley experience, from Fortune 500 companies to tech start-ups. His practice is split between corporate securities (venture capital transactions) and IP licensing and strategy, with strong emphasis on advising on digital asset matters: structuring token ecosystems, advising platforms on listing tokens, and advising companies on developing and implementing NFT strategies. He assisted TikTok on its first token drop, and recently worked on a 16z Crypto venture fund-managed drafting team, to create an NFT license template set (similar to CCO licenses).

Application for one hour of general MCLE credit pending with State Bar of California

AGENDA: "What Every Lawyer Should Know about NFTs"

September 29, 2022

12:00 noon – 1:15 p.m.

I. Panel Introductions (5 minutes)

II. Presentations by panelists Olga Mack (Berkeley Law), Melanie Howard (Loeb & Loeb), Mark Radcliffe (DLA Piper) (50-55 minutes)

Topics to be addressed:

- What is an NFT? Do I need to understand blockchain and smart contracts first?
- Do only certain types of companies or products lend themselves to NFT offerings?
- What types of licenses and sales platforms are available for NFT projects?
- Does IP law impact NFT projects? What about UCC Article 2? Other laws?
- What are lessons from major NFT disputes (Nike, Yuga Labs, Miramax, MetaBerkins)?

III. Q & A (10-15 minutes)

IV. Adjourn

"What Every Lawyer Should Know about NFTs"

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Speaker bios

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Brands and NFTs: Licensing and Contracting Considerations

Melanie J. Howard
Client Alerts/Reports April 2022

In November 2021, an online crypto collective paid nearly $3 million to buy a copy of a "story bible" for director Alejandro Jodorowsky's *Dune*, the 1970s film adaptation of the sci-fi novel that famously never was completed.

Shortly after, the crypto group tweeted about its plan to adapt the book into a movie. There was just one problem: Owning a copy of a book gave the group no rights to the actual intellectual property it would need to produce that movie. They were no closer to owning the necessary rights to produce a movie based upon *Dune*'s intellectual property than they were to owning the rights to produce a movie featuring a certain famous cartoon mouse.

The story illustrates the legal and IP issues inherent in the world of Web3. Over the past year, the space has been dominated by the hype about non-fungible tokens (NFTs). While NFTs have been around since at least 2017, they began to boom in popularity in March 2021, hitting an inflection point when auction house Christie's sold an NFT for a digital artwork by artist Beeple for $69.3 million. After that, it seemed a new NFT craze grabbed headlines every week. Video clips of LeBron James dunking sold for more than $200,000; brands from Adidas to Dolce & Gabbana dropped NFT collections, selling out in minutes and netting millions in sales. In all, the NFT market generated more than $23 billion in transactions in 2021, up from just $100 million the year prior.

NFTs represent a convergence of blockchain technology and creative intellectual property. But what exactly is an NFT, and how does the novel technology map onto our current understanding of intellectual property? Beyond that, what can brands do to both leverage and protect their intellectual property as they draft licenses to govern NFT sales and other Web3 transactions?

- ³rief) Introduction to NFTs

A (Brief) Introduction to NFTs

In simple terms, NFTs are often thought of as digital collectibles, a blockchain-infused version of trading cards or Beanie Babies. In technical terms, an NFT is a unique crypto token that is created and managed on a blockchain, a decentralized, public ledger that tracks the ownership and transaction history of anything stored on it. An NFT is a unit (i.e., "block") of data on the blockchain with its own unique identifier.

The main difference between NFTs and cryptocurrency is their interchangeability. Cryptocurrency like Bitcoin is fungible, meaning that one Bitcoin in one person's wallet is the same as one Bitcoin in another person's wallet. In contrast, each NFT is completely unique, and NFTs are not interchangeable. NFTs can be original and scarce, which makes them interesting for their potential applications to digital media.

NFTs also use software code (called smart contracts) that runs on the blockchain to govern actions such as verifying ownership of an NFT, governing the permitted uses of an NFT, handling the transferability of an NFT, or determining whether and how royalties are paid for secondary sales of the NFT. Smart contracts can also be used to link the NFT to any number of other assets, including art, music or other digital files; this can also be applied to physical assets. Today, most of the popular NFT projects link to digital art files and are on the Ethereum blockchain (leveraging its ERC-721 NFT standard).

What Do You Own When You Buy an NFT?

It is important to distinguish between ownership of an NFT—the unique token on the blockchain—and ownership of the asset that may be linked to or associated with that NFT. When someone purchases an NFT linked to an asset, they have not necessarily purchased any intellectual property rights in that underlying asset. The IP of the underlying asset is still governed by traditional intellectual property laws. For instance, under the U.S. Copyright Act, the copyright owner has the exclusive right to reproduce, prepare derivative works of, distribute, perform and display the copyrighted work. The purchase of a work that is protected by copyright (like the Dune book) does not automatically grant the purchaser any of these underlying rights.

Rights or ownership in the asset underlying the NFT transfers to the purchaser only if the owner of that asset expressly transfers those rights in a license agreement along with the NFT purchase.

NFT License: A Survey of Approaches

Surveying the terms and conditions and licenses granted by brands releasing NFT collections reveals a spectrum of approaches to licensing rights in underlying IP. While not comprehensive, the following three main categories are illustrative and informative: (1) a "traditional" approach, where buying an NFT grants the owner no rights in the underlying IP (much like the purchase of a traditional physical product); (2) a middle-ground approach, where some rights are granted in underlying IP; and (3) a "crypto-native" approach, where purchasing an NFT grants the owner full rights in the underlying IP.

Much of the potential and promise of Web3 and NFTs centers on the technology's ability to support creators and community and, through tokens, the ownership by these creators and community members of the value they help create. This spectrum of approaches illustrates how brands can harness this promise while still protecting their own IP.

Adidas 'Into the Metaverse'

In December 2021, Adidas released its "Into the Metaverse" collection, a collaboration with NFT community Bored Ape Yacht Club (more on Bored Ape Yacht Club below) and various crypto artists. The drop was a limited-edition digital collectible that sold out in minutes.

But from an IP perspective, what did those who bought into the collection actually get? The Metaverse's Terms and Conditions state that Adidas maintains all IP ownership, granting NFT buyers only a limited, nonexclusive right to display the underlying asset:

- "You acknowledge and agree that adidas AG owns all legal right, title and interest in and to the Art, and all intellectual property rights therein."
- "Adidas grants you a worldwide, non-exclusive, revocable, royalty-free license, to display the Art for your Purchased NFTs, solely for the following purposes: (i) for your own personal, non-commercial use (for example home display, display in a virtual gallery or as an avatar); or (ii) as part of a marketplace that permits the purchase and sale of your NFTs."

These Terms and Conditions represent a traditional approach to IP ownership in NFTs and the assets linked to NFTs. In short, NFT purchasers receive limited rights to use the asset for personal use (for e[illegible], displaying it as a social media avatar or in a crypto wallet) or sell the NFT on the secondary market. Under this traditional approach, NFTs are another product line or marketing channel through which brands may leverage and monetize their IP.

Many of the recent fashion brand activations in the metaverse fall under this traditional approach, which represents a massive opportunity for fashion brands. The market for video game skins alone is estimated at $40 billion annually; over the past year, brands from Gucci and Balenciaga to Nike and Ralph Lauren have partnered with gaming ecosystems like Roblox and Fortnite to craft new digital branded skins (add-ons that let players customize their avatars) or virtual experiences. While some of these partnerships have released NFTs, others focused solely on virtual or digital fashion, which are also lucrative. A digital Gucci bag on the gaming platform Roblox recently sold on the secondary market for more than $4,000; (the IRL physical version retailed for $3,400. This bag was not an NFT but simply a digital version of the brand's popular Dionysus Bag with Bee.

Because this approach to leveraging IP is similar to one brands use to create products in the physical world, the brand protection risks are largely analogous to those that established brands face in the IRL marketplace.

Nike and RTFKT

Meanwhile, in December 2021, rival shoemaker Nike acquired digital fashion company RTFKT. Similar to Adidas' terms and conditions, the RTFKT terms state that RTFKT retains all ownership in the underlying asset and grants a limited display right to the purchaser.

Additionally, however, the RTFKT Commercial use license terms permit NFT owners to use the underlying IP of their NFT to create and sell physical merchandise, generating up to $1 million in revenue. With this commercial license option, RTFKT grants two additional rights as compared to the Adidas "Into the Metaverse" collection: a limited right to commercialize the underlying asset, and the right to create derivative works.

These additional rights offer a middle ground between a traditional approach to IP and the crypto-native approach pioneered by collectives like Bored Ape Yacht Club. It represents an evolution beyond the typical fashion brand model of leveraging IP in new markets or product lines, since it allows buyers to build on top of the underlying IP asset to which their NFT ownership is linked.

This middle-ground approach gives potential creators limited license rights to the underlying IP of the NFTs they purchase, allowing brands to harness the potential of Web3 to support creators. However, this a[illegible]h is not without additional legal risk, as the final section of this article will illustrate.

Bored Ape Yacht Club and World of Women

One of the more publicized NFT projects to date has been the Bored Ape Yacht Club, an NFT collection of 10,000 unique "Bored Ape" NFTs. Celebrities including Jimmy Fallon, Paris Hilton and Eminem have all acquired their own Bored Apes. Brands including Adidas have jumped on the Bored Ape trend as well, acquiring their own Bored Ape NFTs. Unlike many of the NFT collections released by established brands, Bored Ape Yacht Club has taken a different approach to IP; when someone purchases a Bored Ape NFT, they own the NFT as well as the underlying asset and IP.

From the Bored Ape Yacht Club's Terms & Conditions:

- "Each Bored Ape is an NFT on the Ethereum blockchain. When you purchase an NFT, you own the underlying Bored Ape, the Art, completely. Ownership of the NFT is mediated entirely by the Smart Contract and the Ethereum Network: at no point may we seize, freeze, or otherwise modify the ownership of any Bored Ape."
- Yuga Labs LLC grants you an unlimited, worldwide license to use, copy, and display the purchased Art for the purpose of creating derivative works based upon the Art."

Since buying a Bored Ape NFT gives the buyer full intellectual property ownership rights, owners have jumped at the chance to turn their Bored Apes into all kinds of media projects, including movies, music, podcasts, books and streetwear. Some owners have even signed their Bored Apes to traditional talent agencies and music labels as an additional intellectual property asset.

Also in this category of approach to IP ownership is World of Women, an NFT project launched in 2021 and featuring 10,000 unique pieces of artwork. World of Women's mission is focused on representation, inclusivity and equal opportunities in crypto. The artwork features women from around the world, each created by a female artist. Like Bored Ape Yacht Club's Terms & Conditions, the World of Women Digital Ownership Agreement grants NFT purchasers full rights in and ownership of artwork linked to the purchased NFT:

"Creator hereby assigns, on an exclusive basis, for the legal duration of the intellectual property rights and for the whole world, all exploitation, reproduction, representation and adaptation rights relating to the Art attached to the Purchased NFT to which this Agreement is linked. It is specified that the rights of reproduction, representation and adaptation are granted to the [NFT owner] for all modes of exploitation, including commercial ones, and on all medium and/or media."

This approach has already garnered the interest of media companies looking to develop the rights granted in this agreement. Reese Witherspoon's Hello Sunshine media company recently entered into a partnership with World of Women that promises to create films, TV, events and other storytelling.

Projects leveraging the intellectual property of NFT collectives like Bored Ape Yacht Club and World of Women illustrate how this crypto-native approach can unleash the full opportunity of crypto communities and creators to use the IP they own in ways that a single-brand house might never have had the vision or resources to realize on its own. Unlike long-established brands like Nike and Adidas, Bored Ape Yacht Club and World of Women are new, crypto-only efforts, making adoption of a crypto-native approach integral to their success.

Unfortunately, It Is Not Risk Free

Of course, both the middle-ground approach and the crypto-native approach—giving NFT owners rights to the underlying assets that have been minted—also come with increased brand protection risks.

First, brands don't have a traditional licensor-licensee relationship with the buyers of their NFT collections, especially when dropping larger collections. For instance, the Adidas "Into the Metaverse" collection included 30,000 NFTs. While this collection did not grant NFT buyers any rights in the underlying IP, the difficulty of policing all the projects and derivative works created if a collection of this magnitude did grant IP rights would be nearly impossible for any brand to manage.

When licensing buyers IP rights in the NFTs—such as to commercialize or to create derivative works—it is imperative to set out clearly in the terms and conditions the scope of permissible uses as well as restrictions on use.

For example, the NFT License, developed by Dapper Labs (creators of CryptoKitties and NBA Top Shot, among other NFT projects), aims to create a standard license that grants NFT buyers certain IP rights in the NFT. In addition to personal use, the NFT License grants owners limited commercial use rights. The license also sets out a number of clear use restrictions, among others, prohibiting owners from using their NFT IP for promoting hatred, intolerance, violence or cruelty; promoting other third-party products or services; or producing movies, videos or other media. If NFT owners violate these provisions, the original creator of the NFT can terminate the agreement.

Practically, it might be difficult for a brand to repossess an actual NFT as a consequence of a purchase violating the underlying license. But since a brand's license agreements govern the NFT owner's rights wi[illegible]spect to the underlying assets of the NFT, drafting clear licenses that are presented to buyers and e[illegible]ccessible becomes important for protecting a brand's IP. For example, the NFT License is drafted in plain language, and it also includes "Intro" and "FAQ" tabs that clearly explain what uses the license does and does not allow.

Somewhat controversially, platforms like OpenSea that allow the buying and selling of NFTs have also frozen the trading of NFTs that were reported as stolen. Given this precedent, it's also important for brands to review the terms of use of these platforms for the potential remedies they may provide against bad actors when deciding where their NFTs might be made available for sale. Of course, brands will also have to police each NFT platform for potential IP infringement. For example, Nike and Hermes have both filed federal lawsuits challenging the creation, marketing and sale of NFTs incorporating their trademarks and trade dress. These lawsuits have the potential to set the precedent for how laws will govern the use and enforcement of branding assets in Web3.

Finally, brands need to understand from a reputational standpoint that many have voiced environmental concerns associated with blockchain mining, which is the process used to validate new transactions (such as NFT sales) on the Ethereum blockchain. While Adidas' acquisition of a Bored Ape NFT went largely without scrutiny, that has not been the case for every brand. Like Adidas, MeUndies also purchased a Bored Ape NFT, but it faced swift customer backlash for the well-documented environmental impact of the Ethereum blockchain (which the Bored Ape Yacht Club uses), with criticism pointing out that the brand has frequently touted its sustainable and environmentally friendly practices. At a time when digital and sustainability present some of the biggest opportunities for growth (particularly for the fashion industry), brands must work to ensure that their digital efforts do not run contrary to their efforts in sustainability.

Crypto Conclusions

Web3 and the recent explosion in the popularity of NFTs present opportunity and promise for established brands to leverage their IP in new and exciting ways. While traditional approaches to IP adapted to the metaverse and NFTs present risks that are familiar to brands that have long worked to protect their IP IRL, crypto-native approaches that seek to engage the creators and community that represent the promise of Web3 will present brands with new risks. As brands experiment with crypto-native approaches, they must adopt strategies to mitigate the risks associated with granting intellectual property rights to NFT owners.

Click here to download a PDF of the full alert.

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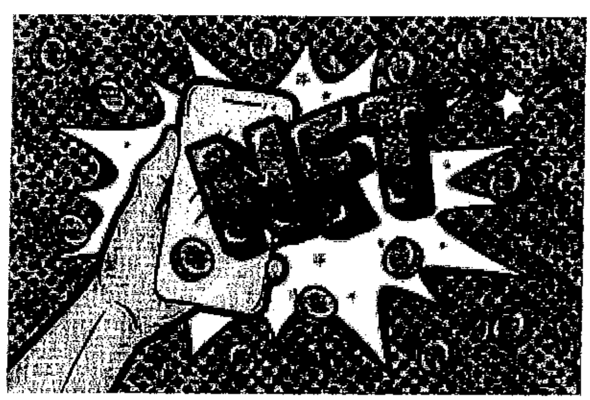
What Do You Need To Know When It Comes To NFTs And The Law?

As NFTs become more popular, it's important to understand the legal issues surrounding them.

By OLGA V. MACK

Jul 18, 2022 at 1:03 PM



As the world of virtual reality continues to grow, so does the potential for digital assets and virtual property. Non-fungible tokens (NFTs) are one kind of such digital asset, and they have quite a promising future. But, as is the case with any new technology, they are accompanied by plenty of legal questions that need to be answered.

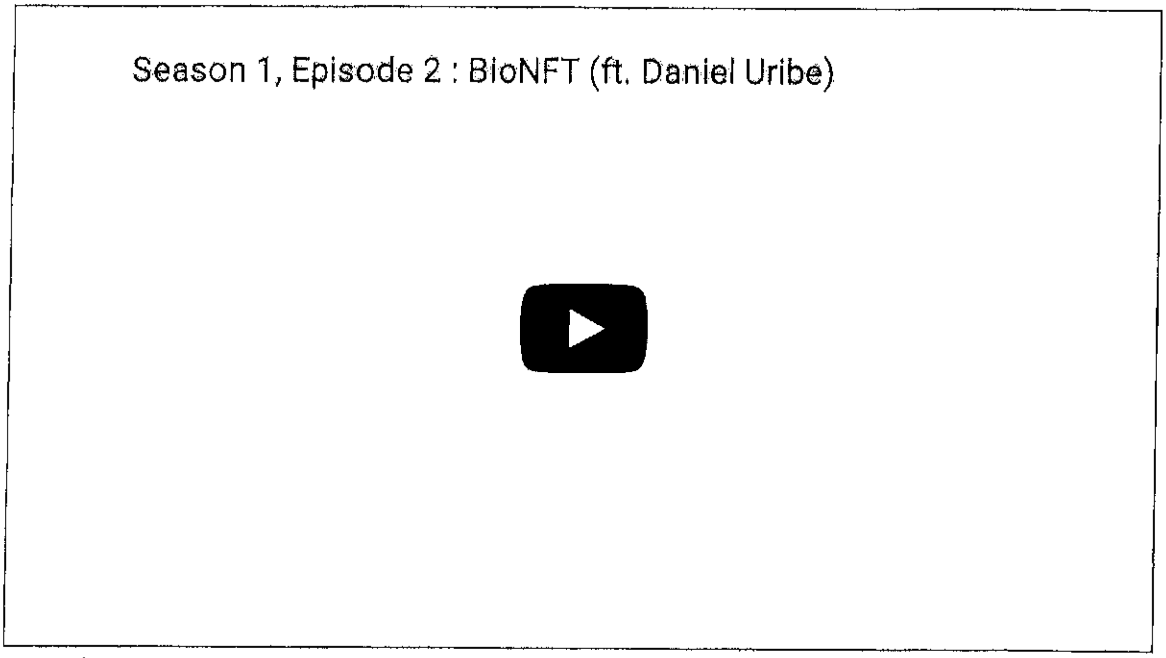
NFTs are unique digital assets that cannot be replicated. They're often used to represent items in games or other virtual worlds, but they can also take the form of art, music, and even physical objects.

Check out the Blockchain Value Season 1, Episode 3 podcast: NFTs — Keeping it Legal! with Jim Gatto.

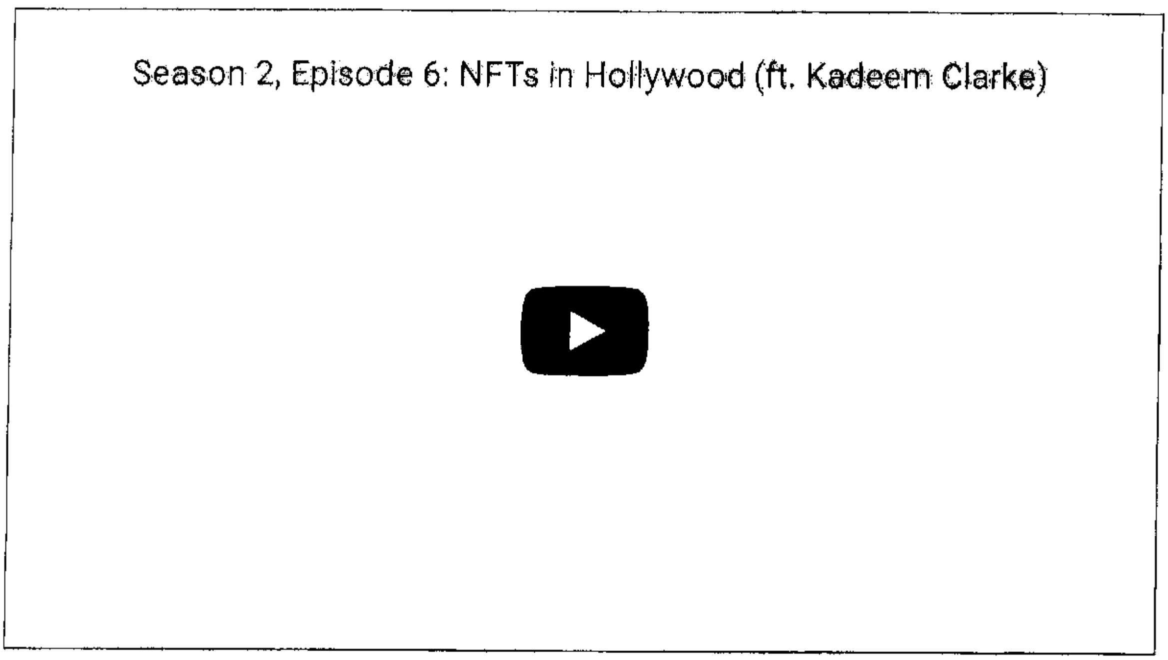
Season 1, Episode 3: NFTs - Keeping it Legal! (ft. Jim Gatto)

While NFTs have a lot of potential, their legal concerns are factors that must be considered. For example, there are questions about who owns NFTs, how they can be taxed, and what happens if they're stolen or lost.

Check out the Blockchain Value Season 1, Episode 2 podcast: BioNFT with Daniel Uribe.



Also check out the Blockchain Value Season 2, Episode 6 podcast: NFTs in Hollywood with Kadeem Clarke.



As NFTs become more popular, it's important to understand the legal issues surrounding them. Here's what you need to know.

What Are NFTs?

NFTs are digital assets, though they are not interchangeable like traditional cryptocurrencies. This means that each NFT has its own unique value that cannot be replicated. An NFT can represent anything from digital artwork to assets found in virtual worlds.

Their unique nature means that NFTs are not subject to the same price fluctuations as traditional cryptocurrencies. Instead, NFT prices are based on supply and demand.

The use of NFTs is still in its early stages, but already a number of platforms enable users to buy, sell, and trade NFTs, including OpenSea, Rarible, and SuperRare.

What Are The Legal Issues Associated With NFTs?

There are a number of different kinds of legal issues that need to be considered when it comes to NFTs.

- **Data Hosting And Storage**

When an NFT is created, the file is stored on a blockchain. This raises multiple issues, including questions of who owns the data, who is responsible for storing it, and how it will be accessed and controlled. There are also concerns about the security of the data and whether it could be hacked or tampered with.

- **Intellectual Property**

Intellectual property is another legal issue that comes into play when NFTs are involved. This includes questions about who owns the intellectual property rights for the NFT and how those rights can be protected.

It's also important to consider how NFTs can be used to infringe on someone else's intellectual property rights. For example, if an NFT is created that uses copyrighted artwork without permission, that could be considered copyright infringement.

- **Royalties**

Since the dawn of the digital age, intellectual property has been a highly debated topic. With the advent of blockchain technology and non-fungible tokens (NFTs), that debate has only intensified.

NFTs have the potential to upend traditional perspectives of intellectual property ownership and royalties. For example, an NFT could be created that gives the owner the right to receive royalties every time the NFT is sold, which could create a whole new revenue stream for artists and other kinds of creators.

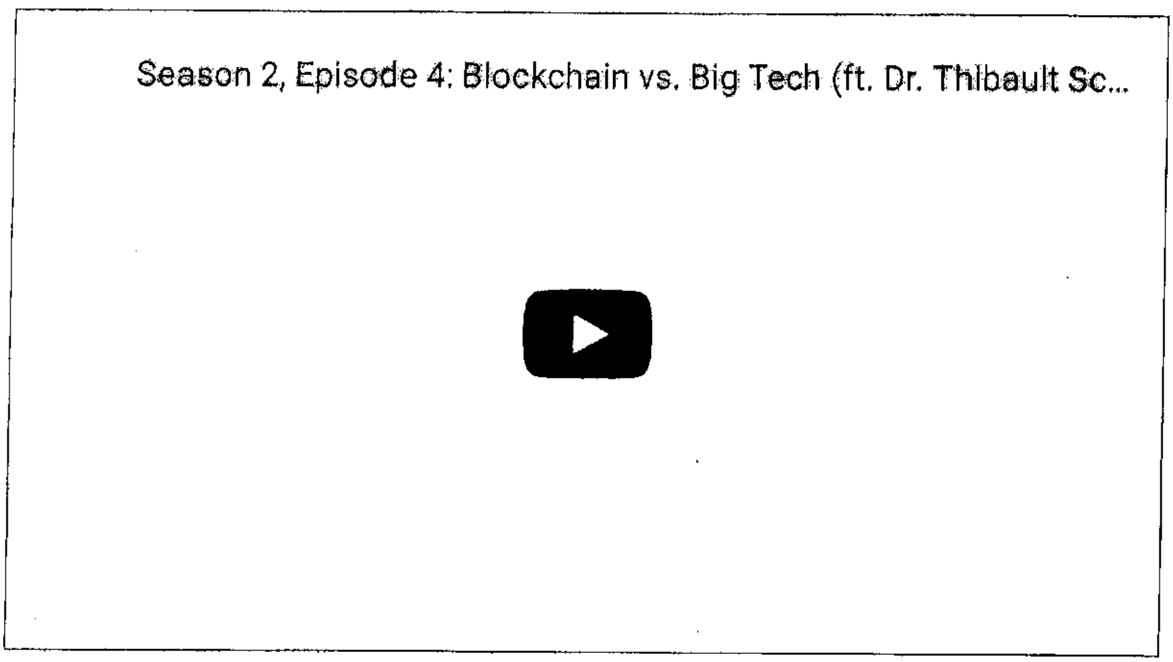
- **Antitrust**

NFTs have the potential to concentrate power in the hands of just a few large companies. If a company were to control the platform on which an NFT is created, they could use that control to stifle competition or raise prices.

Antitrust laws are designed to protect competition and ensure that consumers have access to a variety of choices. If NFTs lead to the conglomeration of power amongst a few companies, that could violate these laws.

It's still the early days of NFTs, so it's hard to say how they will impact the competitive landscape. Nevertheless, antitrust regulators will be watching them closely.

Check out the Blockchain Value Season 2, Episode 4 podcast: Blockchain v. Big Tech with Dr. Thibault Schrepel.



- **Data Privacy**

As interest in buying and selling NFTs grows, there are bound to be concerns about data privacy. After all, NFTs are digital assets that can be stored on a blockchain, which means that the NFT's transaction history is public — accessible to anyone.

This could pose a problem for those wishing to keep their NFT purchases private. For example, someone buying an NFT related to a sensitive topic (such as pornography or political activism) may not want their name attached to that purchase.

There are a few ways to avoid this issue. First, people can use pseudonyms when buying and selling NFTs. Second, there are NFTs that are not stored on a blockchain (such as those stored on centralized servers). Also, people can seek out NFTs with built-in privacy features (such as those using zk-SNARKs).

Of course, data privacy is not an issue unique to NFT buyers and sellers. It is also an issue for any platforms that facilitate NFT transactions. For example, OpenSea — one of the largest NFT marketplaces — recently came under fire for selling user data to third-party advertisers.

- **Financial Regulation**

NFTs are currently unregulated in most jurisdictions, meaning that there is a risk they could be used for money laundering or other illegal activities. However, this lack of regulation is not solely a bad thing, as it also means there is more potential for innovation and creativity.

A few countries' regulations for NFTs are starting to take shape. For example, in the United States, the Securities and Exchange Commission has said that some NFTs could be considered securities, which would subject them to federal securities laws; in China, the central bank has reportedly issued a warning about the risks associated with NFTs.

For the most part, however, NFTs still exist in a legal grey area. This could change as more countries and jurisdictions start taking closer looks at this new technology.

- **Taxes**

When it comes to NFTs, taxes are currently a bit vague. The IRS guidance is minimal. Thus, there is some uncertainty about how to handle them from a tax perspective. If your clients (or you!) are thinking about buying or selling NFTs, it is important to consult a tax professional to ensure you are complying with every applicable tax law.

Olga V. Mack is the CEO of Parley Pro, a next-generation contract management company that has pioneered online negotiation technology. Olga embraces legal innovation and had dedicated her career to improving and shaping the future of law. She is convinced that the legal profession will emerge even stronger, more resilient, and more inclusive than before by embracing technology. Olga is also an award-winning general counsel, operations professional, startup advisor, public speaker, adjunct professor, and entrepreneur. She founded the Women Serve on Boards movement that advocates for women to participate on corporate boards of Fortune 500 companies. She authored Get on Board: Earning Your Ticket to a Corporate Board Seat and Fundamentals of Smart Contract Security. You can follow Olga on Twitter @olgavmack.

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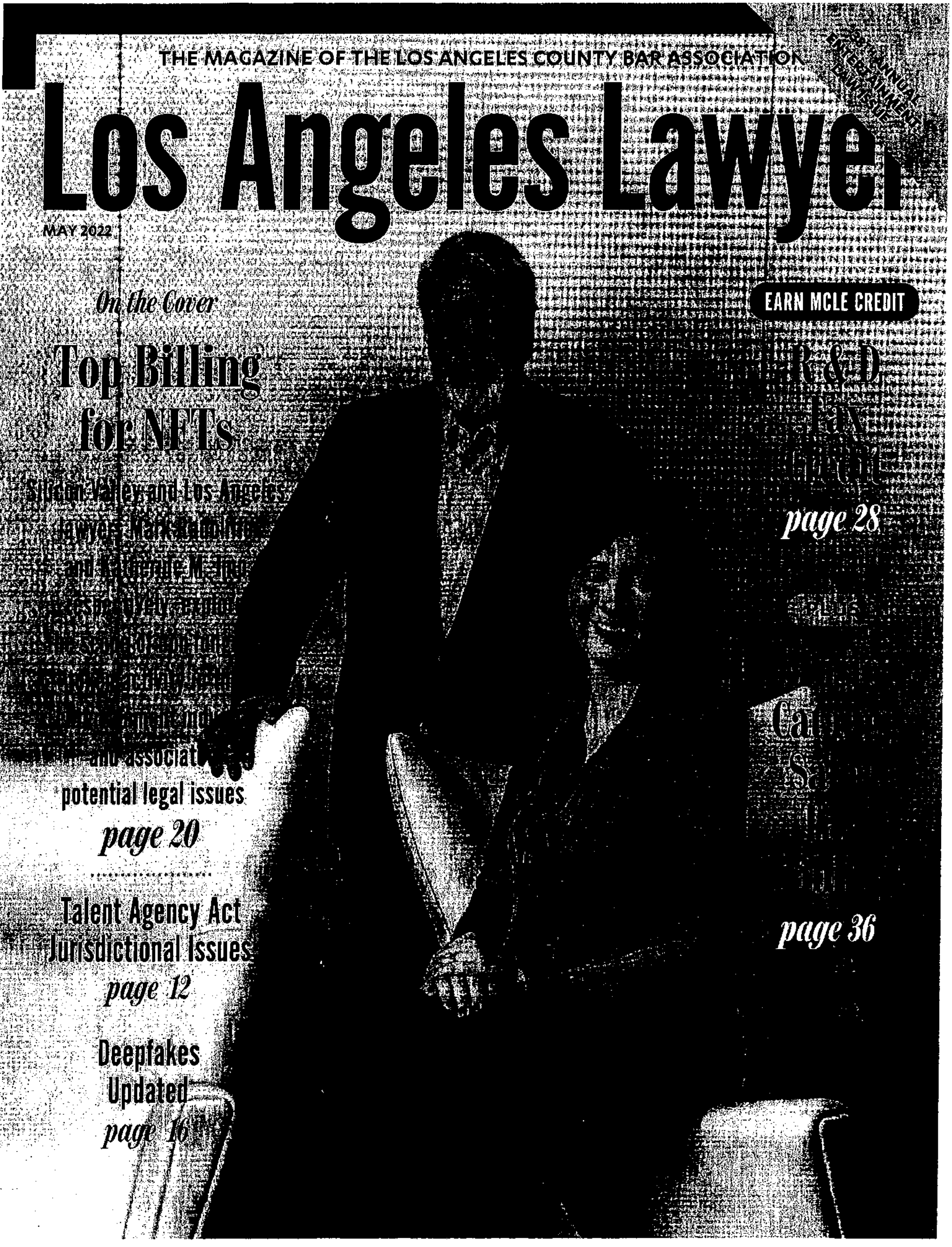
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Often in a young market like that of NFTs, players lose sight of intellectual property rights' savvy as the key to survival

Top Billing for NFTs

BY MARK RADCLIFFE AND KATHERINE M. IMP

NON-FUNGIBLE TOKENS (NFTS) offer enormous opportunities for traditional entertainment companies from new revenue streams to developing direct relationships with their fan communities. However, NFTs also pose risks to traditional entertainment industry business models by enabling artists and new entrants to raise capital and organize more efficiently. The Sales of NFTs have expanded dramatically in 2021 with sales exceeding $22 billion according to DappRadar.[1] Moreover, *Collins English Dictionary* declared "NFT" the word of the year for 2021, and use of the word in 2021 increased more than 11,000 percent over 2020.[2] *Collins* defines an NFT as "a unique digital certificate, that is used to record ownership of an asset such registered in a blockchain, as an artwork or a collectible." NFTs will be critical to the digital strategy

Mark Radcliffe is co-chair of the Digital Asset and Blockchain practice at DLA Piper LLP in Silicon Valley and assists clients with corporate securities and intellectual property transactions. Katherine M. Imp is a transactional media and entertainment attorney in the firm's Century City office.


HADI FARAHANI

for all consumer companies, from movie companies to sport teams to consumer product companies. Many major companies have already started to implement their NFT strategies, including Legendary Pictures,[3] TikTok, and the NFL.

The rise of this novel NFT technology also is permitting new companies to develop businesses based on NFTs and compete with traditional entertainment businesses. One of the best known of these new companies is Bored Ape Yacht Club (BAYC) developed by Yuga Labs LLC,[4] which started as a collection of 10,000 JPEG images of cartoon apes but is expanding into other markets. The company was launched in April 2021 at an average sales price of $186 for a single BAYC NFT. At the end of February 2022, its market capitalization was estimated to be $1,073,506,022,[5] with an average sales price of $282,000 for a single BAYC NFT.[6] Many owners of BAYC NFT use the image as their profile pictures on Twitter, but owners are also permitted to commercialize their NFT image, so BAYC hoodies, t-shirts, and even wine are now available. In addition, the ownership of a BAYC NFT provides access to certain virtual spaces and "special" parties at conferences. The BAYC roadmap includes a blockchain game[7] and, potentially, an animated movie.[8] Yuga Labs LLC, the startup behind Bored Ape Yacht Club, raised $450 million at a post-money valuation of $4 billion by Andreessen Horowitz.[9] While many investors have funded NFT platforms, individual NFT projects like BAYC have not yet received the same kind of investment. Yuga Labs generates revenue primarily via sales of its ape images and other NFTs, plus residual revenue when those NFTs are resold on the blockchain.[10]

Non-fungible token technology will enable artists and celebrities to interact directly with their fans and, potentially, receive a regular income stream through royalties on subsequent resales, or "secondary sales," of the NFTs. The Kings of Leon released an NFT album in 2021 that included three types of tokens: one special album package, a second with live show perks, and a third containing exclusive audiovisual art.[11] Justin Blau sold an NFT collection for $11.6, million, musician PelleK received $160,000 in a pre-sale for the "first" NFT album,[12] and Snoop Dogg's recent Stash Box NFT raised $44 million.[13] Superstar disc jockey Steve Aoki stated in an interview that he made more money from NFTs in the last year than he did from advances during an entire decade of making music.[14] In August 2021, Lionel Messi, the soccer star, launched his NFT collection of three digital art pieces—"Man from the Future," "Worth the Weight," and "The King Piece"—with sales raising $3.4 million.[15] A well-known crypto-artist, Pplpleasr, announced a platform, Shibuya, to enable collaborative development and funding of films.[16] The economics of NFT sales puts traditional entertainment business models at risk.

RollingStone noted that NFT success is based on well-designed and managed communities.[17] NFT communities, frequently moderated on social media applications such as Discord or Telegram, enable community members to collaborate with the lead artist or other community members, share ideas, provide guidance about a project's "roadmap," introduce community members to other projects, and encourage purchases of new works, either of the leading artist or other projects. Such collaboration can include meetings in real time as well as on virtual platforms such as Clubhouse and Twitter Spaces. NFTs will also play an important role in digital worlds, described as the "metaverse."[18]

Projects are being organized using NFTs, distributed autonomous organizations (DAO), and other "Web3"[19] technologies to develop traditional media, such as music and films using NFT communities.[20] The Web3 technologies permit the swift organization of communities to focus on a particular project, such as a film or a collection of images, and, potentially, create larger ecosystems around such projects. NFTs dramatically reduce the cost of interacting with large groups of individuals and permit continuing interactions, such as providing new NFTs and special access to events or virtual spaces.

Blockchain Technology

Blockchain and distributed ledger technology offers significant and scalable processing power, high accuracy rates, and high levels of security at a significantly reduced cost as compared with the traditional systems that the technology could replace, such as capital raising and community organization.[21] Even more than other technologies, the technical details of the implementation of NFTs will affect the nature of the legal issues.[22] For example, the digital nature of the artwork in an NFT may mean that the "first sale" doctrine does not apply to transfer of the NFT artwork and may therefore require an explicit right to assign.[23]

In its simplest form, blockchain is a decentralized, distributed ledger on which transactions are pseudonymously recorded. The transaction ledger is maintained simultaneously across a network of unrelated computers or servers called "nodes," like a spreadsheet that is duplicated thousands of times across a network of computers. The ledger contains a continuous and complete record (the "chain") of all transactions performed, which are grouped into blocks. A block is only added to the chain if the nodes—members in the blockchain network with high levels of computing power—reach consensus on the next "valid" block to be added to the chain. A transaction can only be verified and form part of a candidate block that is determined by the "consensus" protocol of the particular blockchain. Currently, the consensus protocol for the most well-known "Level 1" blockchains, Bitcoin and Ethereum, is Proof of Work (PoW) in which nodes run by "miners" compete to solve a highly complex algorithm to verify it (although Ethereum blockchain has announced that it is shifting to a different consensus approach at the end of 2022, i.e., Proof of Stake). In the last several years, a number of other Level 1 blockchains such as Avalanche, Tezos, and Wax have launched using Proof of Stake as a consensus protocol, which is based on voting by the token holders.

A block generally contains the following: the "hash"[24] of the previous block, a summary of the included transaction, and a time stamp. Once information is entered on the blockchain, it is extremely difficult to alter. A blockchain network lacks a centralized point of vulnerability for hackers to exploit, and each block includes the previous block's "hash." Therefore, any attempts to alter any transaction within the blockchain are easily detectable because every block in the chain would be affected.

In other words, blockchain is a self-maintaining database that typically has a "functionality wrapper," or app development platform, on top. Blockchain can be thought of as an operating system for which useful applications or "smart contracts" can be written. Assets and information about transactions can be stored and tracked without the involvement of a typical intermediary, such as a bank or a central authority or some other trusted third party.

A blockchain network may be public and open ("permissionless") like the Internet or structured within a private group like an intranet ("permissioned"). Permissioned blockchains have captured the imagination of a number of institutions because only certain preapproved participants may join them, such as the Aura blockchain launched by LVMH. These blockchains use a variety of means to ensure the identity of parties to a transaction and to achieve consensus as to the validity of transactions. The entities creating the "private" blockchain agree on rules that govern how entries are recorded and under what circumstances they can be modified. Only specific authorized participants are given access and can use the network.

"Token" in the NFT Context

A "token" is software code that resides on a blockchain platform and has multiple potential uses. Tokens have a number of different functions and can range from "interchangeable" tokens referred to as "fungible tokens" to "unique" tokens referred to as "non-fungible" tokens. Tokens can represent a wide variety of items or services, e.g., a sporting event ticket, digital collectibles, reputation points in an online platform, a copy of a song, or shares in a company.

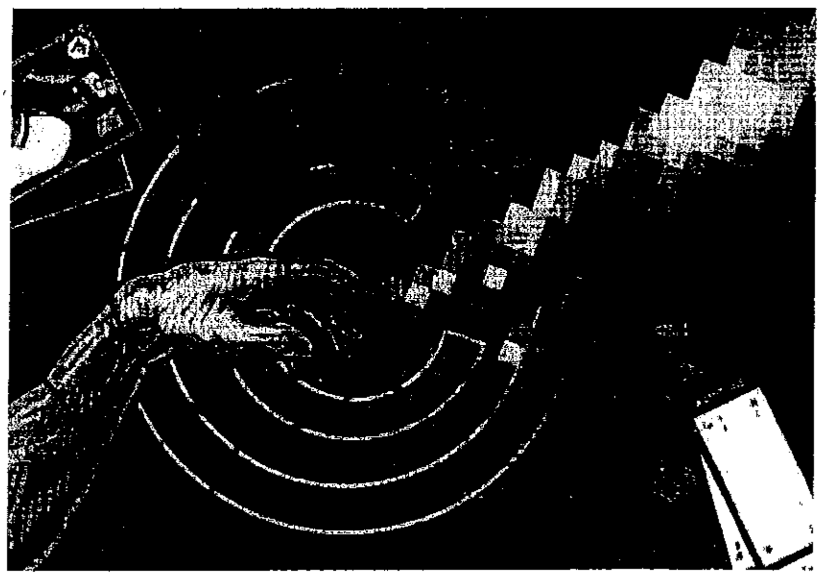
A fungible token is interchangeable with any token of the same type. Bitcoin (BTC) is an example of a fungible token on the Bitcoin blockchain. If you borrow one BTC from a lender, you can pay the lender back with a different BTC, and the lender would be receiving the same value in return. The best known uses for "fungible tokens" are payments. Another major use of fungible tokens is to govern a blockchain protocol through voting rights, such as the Uniswap protocol or the Aave protocol. The standard for fungible tokens on the Ethereum blockchain is ERC 20 (different Level 1 blockchains, such as Tezos and Wax have different standards for these concepts, some of which may be compatible with the ERC standards).[25]

An NFT differs from fungible tokens, because each NFT is unique and not fungible. Each NFT can be uniquely identified. As a result, NFTs are particularly well suited to record ownership of a specific asset, whether physical or digital. The standard for non-fungible tokens on the Ethereum blockchain is ERC 721.[26]

A semi-fungible token is a form of token that can be both fungible and non-fungible during its life cycle. For example, a semi-fungible token that represents a ticket to a Rolling Stones concert is fungible with other such tickets on the same date and in the same seating area. However, once the token is redeemed or the concert is ended, the token is non-fungible since it can no longer be exchanged with another similar token, although it may have value as concert memorabilia.

The standard for semi-fungible tokens on the Ethereum blockchain is ERC 1155.[27] This standard was developed by blockchain game developers, Enjin, Horizon Games, and The Sandbox. It is essentially a combination of the ERC-20 (fungible token) and ERC 721 (non-fungible token) standards.

NFTs consist of a token and the metadata, which includes NFT properties and artwork such as images, videos, or music. The metadata (including the artwork) can be stored on the actual blockchain with the token but such storage is very expensive and many NFTs have a token on the blockchain with a "pointer" to off-chain storage such as AWS, Interplanetary File System, or Arweave. One risk to the pointer structure is that the link can be changed or terminated, which disconnects the token from the artwork. For example, the Raccoon Secret Society (RSS) minted a collection of 1000 raccoon avatars. The RSS then changed the links to the tokens from cute avatars of raccoons to raccoon bones as part of the "Apocalypse" project.[28]



NFT Uses in Entertainment

NFTs are used in a number of different markets, with a growing adoption in the entertainment space. Entertainment-related NFTs can take the form of collaborations with popular collectibles, exclusive add-ons from album releases that yield real-world benefits, or scenes from famous or noteworthy shows or events.[29] Successes and failures both have been observed in NFT exploitation within the entertainment space.

Legendary Entertainment announced the release of a series of digital sculptures as NFTs relating to *Dune*, the movie based on the famous science fiction book. The collection was named "Future Artifacts."[30] However, the studio selected a platform based on the Ethereum blockchain, which has been criticized for its use of energy to power its POW consensus protocol. *Dune* fans were very critical of the choice because it was inconsistent with the environmental theme of the book.[31] Thus, Legendary Entertainment suspended the minting of these NFTs.[32]

The book *Dune* was the source of another attempt to exploit the rights in the book. Late in 2021, a group of crypto investors, organized as a DAO (and named the "Spice DAO"[33]), spent about $3 million at an auction run by Christie's to buy a copy of Alejandro Jodorowsky's "Dune Bible" for his proposed 14-hour film version of *Dune* (AJ *Dune* Bible). Christie's estimated that the AJ *Dune* Bible would sell for a price between $27,500 and $44,000. The Spice DAO stated on Twitter that they intended to "make the book public (to the extent permitted by law)" and develop an animated film.[34] A more bizarre proposal in the Spice DAO Discord channel suggested converting the pages of the AJ *Dune* Bible to JPEGs, selling the JPEGs as a collection of NFTs, and then burning their copy of the book.[35] This proposal was quickly rejected. Many of the members of the Spice DAO apparently did not understand that the purchase of a copy of the AJ *Dune* Bible did not give them any rights under copyright protecting the book.

Non-fungible tokens have uses well beyond simply digital collectibles. For Super Bowl LVI, the NFL offered commemorative ticket stubs as NFTs.[36] Each NFT was customized to feature the ticket holder's unique section, row, and seat, "providing a digital keepsake from their Super Bowl experience."[37] Collecting ticket stubs is not a new phenomenon—holding onto a ticket from a sporting event or music concert is something fans do all the time. The NFL's success in offering the ticket stubs as NFTs, however, suggests that fans are open to collectibles that are digital, not just physical. With giants like the NFL moving towards digital collectibles, we are very likely to see similar activity from other sporting events and concert venues looking to enhance the fan experience.[38]

Legal Issues

As the NFT market expands, so too will the number of legal issues that will need to be navigated and addressed. Included among these legal issues are copyright, trademark, Article II of the Unform Commercial Code (UCC-2), anti-money laundering/know your customer (AML/KYC) measures, and securities laws considerations.

Copyrights. Copyrights are the key rights for many NFTs. Copyright protects "original" works of authorship that are "fixed" in a tangible medium of expression.[39] The standard for originality is very low.[40] Copyright would apply both to the "software" token and the video, music, image, or other artwork that forms an NFT. Typical copyrightable works include films, novels, manuals, videos, music, and computer software. Unlike patents, copyrights arise automatically when a work is created and does not require an application to the government.[41] The scope of copyright law extends to works that are substantially similar to the original work.[42]

The owner of copyright under U.S. copyright law has the following exclusive rights to do and to authorize any of the following (subject to certain exceptions): 1) to reproduce the copyrighted work in copies or phonorecords; 2) to prepare derivative works based on the copyrighted work; 3) to distribute copies or phonorecords of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending; 4) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and motion pictures and other audiovisual works, to perform the copyrighted work publicly; 5) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and pictorial, graphic, or sculptural works, including the individual images of a motion picture or other audiovisual work, to display the copyrighted work publicly; and 6) in the case of sound recordings, to perform the copyrighted work publicly by means of a digital audio transmission.[43] The author's rights under the copyright laws of other countries are similar.

Copyright disputes have already arisen in the NFT market. Shawn Carter (aka Jay-Z) had a dispute with Damon Dash over the right to make an NFT of the cover of the *Reasonable Doubt* album. Jay-Z claimed that the copyrights were owned by Roc-a-Fella Records, Inc., which was not controlled by Damon Dash (he owned one-third of the shares), and the dispute is currently being litigated in the Southern District of New York.[44] Moreover, Miramax, LLC sued Quentin Tarantino for breach of contract, copyright infringement, trademark infringement, and unfair competition based on Tarantino's announcement of his intent to sell NFTs of seven "exclusive scenes" from the movie *Pulp Fiction*. The foreword to the collection describes it as containing scenes from the "original, handwritten screenplay" that "has remained a personal creative treasure that Quentin Tarantino has kept private for decades" in which "[e]ach NFT consists of a single iconic scene, including personalized audio commentary from Quentin Tarantino."[45]

Copyright law includes a number of statutory defenses that may be relevant in certain situations with the "fair use" doctrine being the broadest. Once a court finds copyright infringement, the defendant may raise fair use as an affirmative defense, and a court needs to consider four factors to determine if the "use" is fair.[46] Courts note that fair use is complex and "highly fact dependent."[47] A common example of "fair use" is a parody such as the 2 Live Crew rap version of "Oh, Pretty Woman" in which the Supreme Court noted that the romantic words of the original song were changed into "a bawdy demand for sex and a sigh of relief from paternal responsibility."[48]

Two other copyright doctrines may limit the ability of a copyright owner to enforce its rights, particularly in the case of digital renderings of real world objects, such as clothing or handbags: the merger[49] and scènes à faire[50] doctrines.

Trademarks. Trademarks are words, names, symbols, slogans, smells, sounds or devices used by manufacturers of goods or providers of services to identify their goods and services and set them apart in the marketplace.[51] Familiar examples include the golden arches of McDonalds, the "Tiffany Blue" color trademarked by Tiffany & Co., and the word "Google" for Internet searching. Trademarks can endure forever, so long as they are continuously used.

Trademark disputes have already occurred relating to NFTs. Last year, Miramax sued Quentin Tarantino over his NFT collection based on the film, *Pulp Fiction*, alleging, among other claims, that Tarantino infringed upon Miramax's trademark rights by using the *Pulp Fiction* trademark without permission.[52] More recently, Hermès, which famously sells high-end Birkin bags, sued digital artist Mason Rothschild for Rothschild's NFT collection titled "MetaBirkens," alleging that Rothschild's success in selling the MetaBirkens NFTs arises from "his confusing and dilutive use of Hermès famous trademarks."[53]

However, just as in copyright, courts have developed limits on the enforcement of trademark rights, in order to protect First Amendment interests and avoid stifling creative expression. The Second Circuit established a two-prong test to determine these limits in the *Rogers v. Grimaldi* decision arising from Ginger Rogers' claim that a movie titled *Ginger and Fred* violated her rights under the Lanham Act.[54] The *Rogers* court sought to balance the public's interest in preventing consumer confusion with the First Amendment interest in encouraging creative expression. An expressive work does not violate the Lanham Act 1) unless the trademark use has no artistic relevance to the underlying work whatsoever, or, if it has some artistic relevance, 2) unless the trademark use explicitly misleads as to the source or the content of the work. Ginger Rogers lost her case. A court recently applied the *Rogers* doctrine to dismiss a claim by AM General LLC that the use of an image of a Humvee vehicle in Activision's *Call of Duty* videogames violates AMG's trademark rights in its Humvees.[55]

UCC-2. Article II of the Uniform Commercial Code applies to "transactions in goods."[56] Although the law has not yet been applied to NFTs, most lawyers believe that it would apply because it has been applied to other virtual goods, such as software. An understanding of Article II is critical for licensing NFTs because it includes a number of "default" provisions that are included in an agreement dealing with transactions in goods unless the terms are properly disclaimed as provided in Article II.[57] Several of these provisions, if not properly disclaimed, could lead to significant damages for NFT sellers: 1) the remedy of "consequential damages" that can include lost profits[58] and 2) warranties of "non-infringement"[59] and "merchantability" (applying only to "merchants" who deal regularly in particular goods).[60] If an NFT seller violates the intellectual property rights of a third party by selling an NFT or collection of NFTs and these remedies are not properly disclaimed, the buyer would have the right to collect damages under the warranty of noninfringement, and such damages could include "lost profits."

AML/KYC. NFTs are also presenting new challenges to regulators' and businesses' AML efforts. Because NFT marketplaces are not explicitly regulated by most global regulatory regimes, many of the NFT marketplaces in existence today do not implement KYC measures to verify the identity of the people who use their services.[61] Recently, the U.S. Department of the Treasury referred to NFTs in its *Study of Facilitation of Money Laundering and Terror Finance through the Trade in Works of Art*[62] and noted:

> Because the value of art is subjective, prices for an individual piece of art can be raised or lowered at will. By using straw bids through shell companies or other third-party entities, potential money launderers can manipulatively bid up or down the price of a work, and then easily hide the exchange of illegitimate funds. The subjectivity of prices also allows for the manipulation of value to affect the tax burden for those who donate the asset for tax purposes. Even if a high-value work of art loses value, it can still be sold at a loss for money not connected to the original illicit proceeds.[63]

By their nature, decentralized systems have difficulty complying with KYC regimes. Many decentralized services are designed to allow users to remain anonymous and keep their personal information private from any central authority.[64] Notwithstanding the desire for anonymity, ID verification will be crucial in encouraging a wider adoption of and investment in NFTs. To prepare for impending regulation, and to prevent money laundering and other criminal activity, some NFT marketplaces have begun to conduct a basic KYC process for all users of their platforms during the onboarding process.[65]

Securities Laws. Although NFTs would appear to be unlikely candidates to be securities, they may be offered in a way that would subject them to regulation as securities. Securities are not limited to traditional forms such as stocks and notes but also include "investment contracts" that can cover a wide variety of transactions. Commissioner Hester Pierce (nicknamed "Crypto Mom" for her support of the crypto industry) warned at the Draper Goren Holm Security Token Summit in March 2021 that "[t]he definition of securities can be pretty broad" and that certain types of NFT sales could be considered securities.[66] She reiterated this warning in December 2021.[67] More recently, sources have noted that the U.S. Securities and Exchange Commission (SEC) is investigating certain NFT projects to determine if they should be regulated as securities.[68]

In the United States, it is illegal to offer or sell securities, unless the offer and sale are made pursuant to an effective registration statement filed with the SEC or are exempt from registration under the Securities Act of 1933.[69] NFTs (like other blockchain digital assets) need to consider whether the manner in which the offering is structured would create a risk that it would be considered an "investment contract."

Most of the SEC enforcement actions relating to digital assets, such as *SEC v. Telegram Group Inc. & TON Issuer Inc.*[70] and *SEC v. Kik Interactive Inc.*,[71] were based on finding that token offerings were "investment contracts" as defined in *SEC v. W.J. Howey Co.*[72] In *Howey*, the U.S. Supreme Court defined an investment contract as a "contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party," which is referred to as the *Howey* Test.

The *Howey* Test is generally broken into four prongs to determine whether there exists 1) an investment of money, 2) in a common enterprise, 3) with a reasonable expectation of profits, 4) derived from the efforts of others. If all four prongs are reasonably satisfied, then an instrument or arrangement constitutes a security. If only one of the prongs is not reasonably satisfied, then the instrument or arrangement is not deemed to be an investment contract.

The *Howey* Test is flexible and reaches "novel, uncommon, or irregular devices, whatever they appear to be."[73] The *Howey* Test "embodies a flexible rather than static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of money of others on the promise of profits."[74] In other words, courts are likely to be expansive in their interpretation of facts to determine whether the instrument or arrangement may meet the requirements of each prong of the *Howey* Test.

NFT Strategy Guidelines

NFTs provide major new opportunities and risks for the traditional entertainment industry. The technology, particularly when combined with other kinds of technology, enables companies and individuals a method to connect with existing customers in new ways from access to special events to a separate experience in a digital world (sometimes called "metaverse"). However, the technology is still nascent, and many legal issues and risks remain unresolved. A company developing its NFT strategy should consider the following issues:

- **Be Prepared to Experiment with Different Strategies.** NFTs have a wide number of potential uses for a company from collectibles like "digital tickets stubs" to access to special events. The sale of NFTs alone does not take advantage of the full possibilities of the technology. The NFT strategy should consider using NFTs to develop a community by using social media, such as Discord or Twitter, as well as real world events as part of the strategy.
- **Intellectual Property Rights Will Be Critical to Success.** If a company intends to use existing content, it should ensure that they have cleared the necessary rights. For example, a video can include music and background works (such as street art) that have a copyright owned by third parties. Since NFTs are likely to become more important in the future, companies should ensure that their agreements include rights to exploit content in NFTs. Also, they should protect their core brands in this new area by registering their trademarks in the appropriate classes and jurisdictions.
- **Monitor NFT Platforms for IP Infringements.** The NFT marketplace is young, and many participants are casual about IP rights or simply do not understand them, like the members of the Spice DAO and their misunderstanding that buying a physical item—the AJ *Dune* Bible—would give them rights nto make movies and other spinoffs. ■

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