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# Mining the NFT Goldrush: A Prospective Guide to Drafting NFT Contracts

DeJuawn “DJ” Griffin\*

## I. INTRODUCTION: “GREATER FOOL” THEORY, “FOOL’S GOLD,” OR SOMETHING MORE?

Nonfungible tokens (NFTs) are an emerging digital asset class that present unique and innovative means of commercialization. Artists and creators “minted”<sup>1</sup> and sold NFTs without much notice until they boomed into the public consciousness in March 2021, hitting an inflection point when Christie’s, a world-leading art and luxury online auction business, made history with the monumental sale of artist Beeple’s *Everydays: The*

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1. Minting is the act of adding, validating, and recording an NFT to the blockchain. Once minted, the NFT is available for public (or private) consumption and can be viewed, bought, and traded on open marketplaces like SuperRare or OpenSea. Randy Ginsburg, *NFT Dictionary: All the Terms and Definitions You Need to Know*, NFT NOW (Apr. 5, 2022), <https://nftnow.com/guides/nft-dictionary-all-the-terms-and-definitions-you-need-to-know/> [https://perma.cc/WP3U-8J4T].

*First 5000 Days*<sup>2</sup> for \$69.3 million.<sup>3</sup> This monumental sale sparked an NFT craze by celebrities, creators, and athletes exploring ways to commercialize their brand, image, or content. Even former Twitter CEO Jack Dorsey sold his first-ever tweet for \$2.9 million as an NFT.<sup>4</sup> Surging past 2020's \$100 million gross, the 2021 NFT market generated more than \$23 billion in transactions.<sup>5</sup>

The market trend over fiscal year<sup>6</sup> 2022 thus far signifies that NFTs are dropping back to their “floor prices,”<sup>7</sup> while the NFT market moves from a “bull market”<sup>8</sup> into a “bear market.”<sup>9</sup> Some economists are comparing this market correction to the seventeenth-century market bubble of Tulip Mania.<sup>10</sup> A market bubble forms when a series of assets

2. *Online Auction 20447 Beeple: The First 5000 Days*, CHRISTIE'S (Mar. 11, 2021), <https://onlineonly.christies.com/s/beeple-first-5000-days/beeple-b-1981-1/112924> [<https://perma.cc/GJ9F-6LKL>].

3. Scott Reyburn, *JPG File Sells for \$69 Million, as 'NFT Mania' Gathers Pace*, N.Y. TIMES (Mar. 25, 2021), <https://www.nytimes.com/2021/03/11/arts/design/nft-auction-christie-beeple.html> [<https://perma.cc/3U4E-4R5A>].

4. Adam Smith, *Jack Dorsey's first tweet sold for \$2.9M as an NFT—but new auction achieves top bid of just \$280*, YAHOO SPORTS (Apr. 14, 2022), <https://sports.yahoo.com/jack-dorsey-first-tweet-sold-103836095.html> [<https://perma.cc/4RVR-X5S9>].

5. Pedro Herrera, *2021 Dapp Industry Report*, DAPP RADAR (Dec. 17, 2021), <https://dappradar.com/blog/2021-dapp-industry-report>.

6. A fiscal year is a one-year period that companies and governments use for financial reporting and budgeting, but not necessarily starting at the beginning of the calendar year. *Fiscal year*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/fiscal%20year> [<https://perma.cc/F98L-CKHF>] (last visited Mar. 14, 2023).

7. See Ginsburg, *supra* note 1 (explaining that “[t]he floor price of an NFT collection is the lowest listed price in the entire collection. The value of a collection is often dictated by its floor price.”).

8. Leslie Kramer, *An Overview of Bull and Bear Markets*, INVESTOPEDIA (May 20, 2022), <https://www.investopedia.com/insights/digging-deeper-bull-and-bear-markets/> [<https://perma.cc/9NKT-VQGU>] (defining a bull market as “a market that is on the rise and where the economy is sound”).

9. *Id.* (defining a bear market as one which “exists in an economy that is receding, where most stocks are declining in value”). See also Elizabeth Howcroft, *NFT sales plunge in Q3, down by 60% from Q2*, REUTERS (Oct. 3, 2022), <https://www.reuters.com/technology/nft-sales-plunge-q3-down-by-60-q2-2022-10-03/> [<https://perma.cc/UU65-X2E8>].

10. Tim Hartford, *Was Tulip Mania really the first great financial bubble?*, BBC (Mar. 4, 2020), <https://www.bbc.com/news/business-51311368> [<https://perma.cc/6J68-RHGY>]. “Tulip Mania” is a term coined by Scottish author Charles Mackay in his piece: *Memoirs of Extraordinary Popular Delusions and the Madness of Crowds*. Essentially, a market bubble formed in February 1637, when one particularly rare bulb—the Semper Augustus—enchanted the Dutch populace and became a popular status symbol for wealthy members of the Dutch Elite. The astronomical prices collapsed as rapidly as they ascended, which caused the Dutch economy to collapse. Tulip Mania is often cited as the classic example of

increase in price dramatically beyond their fundamental value. Opportunistic investors purchase these overpriced assets as a strategy not to accumulate value but to amass profit. Prices continue to rise as investors find “greater fools”<sup>11</sup> to purchase the assets until the bubble bursts and someone is left holding the bag of “fool’s gold.”<sup>12</sup> This explains why Bill Gates, during an event on climate change hosted by TechCrunch, described the NFT phenomenon as “100 percent based on greater fool theory.”<sup>13</sup>

Because this asset class is still in its nascent stage, NFTs are shrouded in layers of legal and regulatory uncertainty and complexity. This stems from what Max Curnin, Co-Founder and Chief Executive Officer of Remaster,<sup>14</sup> describes as the disconnect between hyper-liquidity—the state at which a market’s efficiency and transparency levels are at their highest possible levels—and reactive litigation and regulations.<sup>15</sup> Nevertheless, as the asset class matures, U.S. regulations and courts are catching up to the developing technology in a host of novel and difficult legal issues, ranging from whether the NFTs are securities under the Securities Act of 1933<sup>16</sup> to the scope of copyright licenses for works of art. Currently, entrepreneurs and lawyers are on the cutting edge of drafting contracts or intellectual property rights in the absence of federal and state regulations. Accordingly, this comment discusses recent litigation

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a financial bubble: when the price of something goes up and up, not because of its intrinsic value, but because people who buy it expect to be able to sell it again at a profit. *Supra*.

11. Vicki Bogan, *The Greater Fool Theory: What Is It?*, HARTFORD FUNDS, [http://bogan.dyson.cornell.edu/doc/Hartford/Bogan-9\\_GreaterFools.pdf](http://bogan.dyson.cornell.edu/doc/Hartford/Bogan-9_GreaterFools.pdf) [<https://perma.cc/88HC-VV3M>]. (last visited Mar. 14, 2023).

12. James Chen, *Fool’s Gold*, INVESTOPEDIA (Apr. 26, 2022), <https://www.investopedia.com/terms/f/foolsgold.asp> [<https://perma.cc/Y3SH-4KTD>]. Fool’s gold is “any flashy but ultimately worthless investment . . .” The term originally referred only to iron pyrite, which is commonly mistaken for gold. *Id.*

13. James Vincent, *Bill Gates says NFTs are ‘100 percent based on greater fool theory,’* THE VERGE (June 15, 2022), <https://www.theverge.com/2022/6/15/23169008/bill-gates-cryptocurrency-nft-greater-fool-theory> [<https://perma.cc/W328-AEFC>]. In finance, the “Greater Fool Theory” suggests that one can sometimes make money through the purchase of overvalued assets—items with a purchase price drastically exceeding the intrinsic value—if those assets can later be resold at an even higher price. *See* Bogan, *supra* note 11.

14. REMASTER, <https://remaster.io/> [<https://perma.cc/7WQZ-PFNH>] (last visited Mar. 14, 2023). Remaster is a startup focused on accelerating commerce through legal infrastructure and empowering the Web3 community.

15. Bankless Shows, *IP Lawyers Answer Your Questions about NFTs*, YOUTUBE, at 51:22 (Aug. 18, 2022), <https://www.youtube.com/watch?v=velJ8LsIY4E&t=1s> [<https://perma.cc/JKB5-RYCH>].

16. 15 U.S.C. § 77k.

and endeavors to survey the terms, conditions, and licenses granted by brands and provide a spectrum of approaches to drafting strong, comprehensive licensing NFT agreements for investors, law firms, and financial technology (Fintech) companies.

## II. NFTS EXPLAINED: THE FEATURES AND FUNCTIONALITIES OF NFTS

Simply put, an NFT is a one-of-a-kind “token,”<sup>17</sup> based on computer code, that is created and managed on a “distributed ledger,”<sup>18</sup> commonly known as blockchains,<sup>19</sup> that signals a record of ownership for digital assets.<sup>20</sup> Today, NFTs are primarily minted on the “Ethereum”<sup>21</sup> blockchain, in the “Web3 economy,”<sup>22</sup> written in the “Solidity”<sup>23</sup> programming language. Once minted, NFTs effectively become a permanent part of that blockchain.<sup>24</sup> Clear as mud, right?

17. A “token” is also a set of encrypted code created by a blockchain but can be used for applications other than, but including, virtual money—for instance, to open programs or applications or access services. *Definition of a security: Statutory and case law; cryptocurrencies: coins and tokens; non-fungible tokens—NFTs*, SEC.: PUB. & PRIV. OFFERINGS § 1A:11 (2d ed. 2022).

18. See Aaron Wright & Primavera De Filippi, *Decentralized Blockchain Technology and the Rise of Lex Cryptographia*, SSRN (Mar. 20, 2015), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2580664](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2580664) [<https://perma.cc/WKG5-GVZS>]. “The blockchain is a distributed, shared, encrypted-database that serves as an irreversible and incorruptible public repository of information. It enables, for the first time, unrelated people to reach consensus on the occurrence of a particular transaction or event without the need for a controlling authority.” *Id.* at 2.

19. See Bennett Garner, *Merkle Tree Hashing: How Blockchain Verification Works*, COINCENTRAL (Sept. 3, 2018), <https://coincentral.com/merkle-tree-hashing-blockchain> [<https://perma.cc/7RU4-YB2A>] (writing that in a bitcoin blockchain, a block of transactions runs through an algorithm to generate a hash which can then be used to verify “the contents of the block and consistency of multiple ledgers.”).

20. See Ginsburg, *supra* note 1.

21. Ethereum is a blockchain platform that allows for securely processing peer-to-peer transactions. Many popular art NFTs are part of the Ethereum blockchain due to the platform’s smart contract functionality. ETHEREUM, <https://ethereum.org/en/> [<https://perma.cc/9AKA-S3WF>] (last visited Mar. 14, 2023).

22. Web 3.0 refers to the third evolution of web technologies and encompasses the decentralized applications that run on blockchains. Gilad Edelman, *The Father of Web3 Wants You to Trust Less*, WIRED (Nov. 29, 2021), <https://www.wired.com/story/web3-gavin-wood-interview/> [<https://perma.cc/BZS7-8P5L>].

23. Solidity is a statically typed curly-braces programming language designed for developing smart contracts that run on Ethereum. SOLIDITY, <https://soliditylang.org> [<https://perma.cc/SQ8W-XR6P>] (last visited Mar. 14, 2023).

24. Andy Storey, *Is It Possible for an NFT to be Destroyed*, POSTER GRIND (Dec. 17, 2021), <https://postergrind.com/is-it-possible-for-an-nft-to-be-destroyed/> [<https://perma.cc/4X4C-NWNR>]. NFTs are permanent because they can only be “destroyed” by sending it to

By its terms, NFTs consists of two distinct parts: nonfungible and token. NFTs are “nonfungible”<sup>25</sup> because each NFT has its own unique identification code and “metadata”<sup>26</sup> that cannot be replaced or substituted by an identical version of the digital asset.<sup>27</sup> It is akin to one-of-one paintings or trading cards, like the 2002 Pokémon World Championships “*No. 1 Trainer*”<sup>28</sup> card. On the other hand, bitcoin or other cryptocurrencies are “fungible” goods because they are identical and are readily exchangeable for equal value.<sup>29</sup> Cryptocurrency is a “coin”<sup>30</sup> that can be purchased or converted into fiat currencies, such as dollars, euros, or yen, through crypto exchanges for blockchain transactions.<sup>31</sup>

In contrast, tokens are assets that are digitally transferrable between two parties in the “blockchain ecosystem,”<sup>32</sup> which can be assigned specific uses and properties. The token is personal property which grounds the property interest. It is both real-world and digital property.<sup>33</sup> Tokens provide access to and are used to interact with decentralized

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an address from which it cannot be transferred, rendering it inaccessible—a process called “burning” an NFT. The NFT remains on the blockchain, but the economic value is destroyed by making it impossible to sell. *Id.*

25. *Non-fungible token*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/non-fungible%20token> [<https://perma.cc/H8U6-MX2Q>] (last visited Mar. 14, 2023).

26. Metadata provides information about the digital work associated with an NFT. This often includes its title, a description of the work, and a link to its primary assets, such as the image file. *The A-Z of NFT: artists and terminology to know*, CHRISTIE’S (Sept. 27, 2022), [https://www.christies.com/features/a-to-z-nft-collecting-guide-12425-1.aspx?sc\\_lang=en](https://www.christies.com/features/a-to-z-nft-collecting-guide-12425-1.aspx?sc_lang=en) [<https://perma.cc/8B7L-GAGD>].

27. See *Non-fungible token*, *supra* note 25.

28. Matt Jarvis, *Top 15 Most Rare and Expensive Pokémon Cards*, DICEBREAKER (Feb. 22, 2023), <https://www.dicebreaker.com/games/pokemon-trading-card-game/best-games/rare-pokemon-cards> [<https://perma.cc/SFT8-AXGW>].

29. *Fungible*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/fungible> [<https://perma.cc/YVY4-B92G>] (last visited Mar. 14, 2023).

30. See *Definition of a security: Statutory and case law; cryptocurrencies: coins and tokens; non-fungible tokens—NFTs*, *supra* note 17 (defining a coin as “a set of encrypted code representing crypto currency or digital money [that] is generated and captive to the blockchain that created the ‘coin.’”).

31. *Cryptocurrency*, MERRIAM-WEBSTER, <https://www.merriam-webster.com/dictionary/cryptocurrency> [<https://perma.cc/F76C-DSPC>] (last visited Mar. 14, 2023).

32. Anusha Meghawat, *A Beginners Guide to understand the Blockchain Ecosystem*, ANALYTICS VIDHYA (Aug. 7, 2022), <https://www.analyticsvidhya.com/blog/2022/08/a-beginners-guide-to-understand-the-blockchain-ecosystem/> [<https://perma.cc/BW7K-UVJZ>].

33. Joshua A.T. Fairfield, *Tokenized: The Law of Non-Fungible Tokens and Unique Digital Property*, 97 IND. L.J. 1261, 1312 (2022).

applications (dApps),<sup>34</sup> like “OpenSea”<sup>35</sup> or “Magic Eden,”<sup>36</sup> that incorporate NFT use into the software in the NFT marketplace.<sup>37</sup> Decentralized applications are powered by “smart contracts,”<sup>38</sup> an identifier that is a bit of a misnomer.<sup>39</sup> The idea was that a smart contract would replace the legal instrument of a traditional contract through an automatically executable program.<sup>40</sup> However, not only is there no legal language in a smart contract, but it also does not function as a legal document.<sup>41</sup> Nor can they be contract substitutes.<sup>42</sup>

Contracts are bargains for exchange described in expressly stated terms, not in code.<sup>43</sup> Contracts involve the creation of reciprocal legal obligations and making binding promises.<sup>44</sup> In contrast, smart contracts are programs that create and convey NFTs. Smart contracts are self-executing contracts with the terms of the agreement between buyer

34. Jake Frankenfield, *Decentralized Applications (dApps): Definition, Uses, Pros and Cons*, INVESTOPEDIA (Jan. 9, 2023), <https://www.investopedia.com/terms/d/decentralized-applications-dapps.asp> [<https://perma.cc/7CYZ-JQR8>].

35. OPENSEA, <https://opensea.io/> (last visited Mar. 14, 2023).

36. MAGIC EDEN, <https://magiceden.io/> [<https://perma.cc/GST5-CNKK>] (last visited Mar. 14, 2023).

37. Juliet M. Moringiello & Christopher K. Odet, *The Property Law of Tokens*, 74 FLA. L. REV. 607, 640 (2022).

38. Michael D. Murray, *NFTs And The Art World—What’s Real, And What’s Not*, 29 UCLA ENT. L. REV. 25, 51 (2022) (“Smart contracts are one of the great oxymorons of the 21st century: they are neither smart, nor are they contracts in the legal sense of the term.”); see also Cryptopedia Staff, *Real-World Use Cases for Smart Contracts and dApps*, CRYPTOEDIA (Dec. 23, 2021), <https://www.gemini.com/cryptopedia/smart-contract-examples-smart-contract-use-cases> [<https://perma.cc/XR7H-S2T8>].

39. Harry Surden, *Computable Contracts*, 46 U.C. DAVIS L. REV. 629, 639–40 (2012) (differentiating between traditional contracts memorialized with words and data-oriented contracts memorialized in computer data).

40. *Id.* at 640.

41. *Id.*

42. Nick Szabo, *Formalizing and Securing Relationships on Public Networks*, FIRST MONDAY (Sept. 1, 1997), <https://firstmonday.org/article/view/548/469> (defining the hallmark of contract formation as a “set of promises agreed to in a [mutual] ‘meeting of the minds,’” which smart contracts may not fulfill).

43. Kevin Werbach & Nicolas Cornell, *Contracts Ex Machina*, 67 DUKE L.J. 313, 356 (2017) (“[O]ne might suggest that smart contracts, by making performance inevitable, are no longer promises at all . . . . Whereas contract law supports promising by giving promisors legal reasons to perform, smart contracts do away with the need for reasons altogether[.]”).

44. *Raffles v. Wichelhaus* (1864) 159 Eng. Rep. 375, 376 (Exch.) (finding that no contract is formed when both parties mutually misunderstand the meaning of a term of agreement).

and seller being directly written into lines of code.<sup>45</sup> Once a smart contract has been created, computer transaction protocols will execute the terms of a contract automatically based on a set of conditions.<sup>46</sup> To better understand this concept, consider a vending machine, which is programmed to verify that enough money has been deposited before dispensing a candy bar without the need for an intermediary or central authority.

For example, when someone purchases an NFT linked to a digital artwork, the NFT is minted and traded using a smart contract that executes the “on-chain”<sup>47</sup> sale by assigning or transferring ownership rights, assessing assets within the NFT, recording those rights on a non-replicable distributed ledger, and, hopefully, allocating proceeds from that transaction. In terms of deliverables, the purchaser would then own a unique location on the Ethereum blockchain that points to a text file published on a temper-proof ledger embodying the publicly hosted image. But, of course, the NFT could involve more than just an image. Although they are analogous to contracts functionally, it is important to not conflate smart contracts with the features of traditional legal contracts or licensing agreements. The former are computer programs that automate the enforcement of codified terms, whereas the latter are sets of agreed-upon terms which are enforceable by law and are described in a natural, mortal language.<sup>48</sup>

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45. Tsui S. Ng, *Blockchain and Beyond: Smart Contracts*, AMERICAN BAR ASSOCIATION (Sept. 28, 2017), [https://www.americanbar.org/groups/business\\_law/publications/blt/2017/09/09\\_ng/](https://www.americanbar.org/groups/business_law/publications/blt/2017/09/09_ng/) [<https://perma.cc/4X9N-L7CZ>].

46. *Id.*

47. On-chain refers to a digital token that lives on a blockchain. This term is also used to represent any transaction or interaction with a token or contract on the blockchain. Devin Finzer, *The Non-Fungible Token Bible: Everything you need to know about NFTs*, OPENSEA BLOG (Jan. 10, 2020), <https://blog.opensea.io/guides/non-fungible-tokens/> (“The benefits of representing metadata on-chain are: [(1) it permanently resides with the token, persisting beyond the lifecycle of any given application, and [(2) it can change in accordance with on-chain logic. Point #1 is important if assets are intended to have long-lasting value far beyond their original creation. For example, a piece of digital art is expected to persist throughout the ages, regardless of whether the original website that was used to create the art is still around.”).

48. Charles Fried, *Contract as Promise: A Theory of Contractual Obligation*, 81 MICH. L. REV. 904, 905 (1983) (“Promise transforms a choice that was once morally neutral into one that is morally compelled[.]”).



### III. THE “WILD WEST” OF NFTS: A HISTORICAL OVERVIEW OF THE NFT

While NFTs seem like they have arrived out of nowhere, they do trace back a few short years. The history leading up to mainstream use of the Ethereum blockchain is rich with data going back a decade. Since then, there has been a lot to happen with NFTs and the Ethereum blockchain. Although the ultimate impact of NFTs on business and culture remains to be seen, their growing popularity warrants anyone with a curious mind to take a deeper look into the existing ecosystem. This journey is a long story with many people, artists, and projects involved, so let’s dive in, fellow “NFT archaeologists.”<sup>49</sup>

#### A. *The Past: The NFT Frontier Period (2012–2016)*

In 2012, the idea of NFTs emerged from Meni Rosenfeld’s “Colored Coin.”<sup>50</sup> Initially issued on the Bitcoin blockchain for as little as a single “satoshi,”<sup>51</sup> the smallest unit of currency, Colored Coins resembled current NFTs in critical ways. In the *Overview of Colored Coins*, Rosenfeld described the innovative use of the Bitcoin infrastructure creating a new asset class and giving raw possibilities for future utilization.<sup>52</sup> With proper hindsight, the limitations of the Bitcoin blockchain meant that the Colored Coins concept could never be realized. Rosenfeld’s ingenuity, nevertheless, exemplified capabilities that marked the NFT frontier period.

On May 2, 2014, digital artist Kevin McCoy’s *Quantum*<sup>53</sup> was regarded as the first-known NFT ever minted.<sup>54</sup> Unlike most NFTs today, which are minted on Ethereum, McCoy had used a blockchain software called

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49. Jonathan Torrey, *A Conversation With NFT Archaeologists—Wait, What the Heck Is That?*, ONE37PM (June 6, 2022), <https://www.one37pm.com/nft/nft-archaeology-gabagool-adam-mcbride-interview> [https://perma.cc/Q4TM-92TB] (“An NFT archaeologist is . . . interested in understanding the origins of our present phenomenon.”).

50. Meni Rosenfeld, *Overview of Colored Coins* (Dec. 4, 2012), <https://allquantor.at/blockchainbib/pdf/rosenfeld2012overview.pdf> [https://perma.cc/NR26-WNGH].

51. Satoshi’s price today is US \$0.000191. In other words, 1,000 Satoshi is worth \$0.19. *Satoshi*, CRYPTO, <https://crypto.com/price/satoshi> [https://perma.cc/7N28-N8UM] (last visited Mar. 14, 2023).

52. See Rosenfeld, *supra* note 50 at 7–9.

53. *Quantum*, JENNIFER AND KEVIN MCCOY, <https://www.mccoyspace.com/project/125/> [https://perma.cc/SSX4-JV6W] (last visited Mar. 14, 2023).

54. A. Hamilton, *The Beginning Of NFTs—A Brief History Of NFT Art*, ZENO FINE ART (Mar. 6, 2023), <https://www.zenofineart.com/blogs/news/the-beginning-of-nfts-a-brief-history-of-nft-art> [https://perma.cc/K75U-R3EJ].

“NameCoin”<sup>55</sup> to create *Quantum*—a digital image of a pixelated octagon that hypnotically changes color and pulsates in a manner reminiscent of an octopus.

Later that year, Robert Dermody, Adam Krellenstein, and Evan Wagner founded “Counterparty,” a peer-to-peer financial platform, and distributed open-source internet protocol built on the Bitcoin blockchain.<sup>56</sup> Counterparty allowed digital asset creation and had a decentralized exchange, thus providing a way for users to create their own tradable currencies or assets.<sup>57</sup> The idea of tradable collectibles on the blockchain came with a critical advantage not afforded to real-world rare collectible items: counterfeiting was all but impossible. In 2015, Counterparty partnered up with the game creators of *Spells of Genesis* (SoG).<sup>58</sup> SoG pioneered the issuing of in-game assets on the blockchain, introducing its own in-game currency called “BitCrystals.”<sup>59</sup> In 2016, memes entered the blockchain, which beckoned on the age of meme trading and saw the release of a host of *Rare Pepes*<sup>60</sup> NFTs, the Pepe the Frog character, on the Counterparty platform.<sup>61</sup>

During this frontier period, the growth potential of NFTs could not be realized because the Bitcoin blockchain was never intended to be used as a database for tokens representing the ownership of assets. Thus, the big shift to the Ethereum blockchain began.

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55. NAMECOIN, <https://www.namecoin.org> [<https://perma.cc/GH44-5CCV>] (last visited Mar. 14, 2023).

56. COUNTERPARTY, <https://counterparty.io> [<https://perma.cc/AQ47-YNBB>] (last visited Mar. 14, 2023).

57. *Id.*

58. SPELLS OF GENESIS, <https://spellofgenesis.com/> [<https://perma.cc/Q9FD-PTT7>] (last visited Mar. 14, 2023).

59. *Id.* (“Bitcrystals is available on 3 blockchains: (1) BCY (XCP) = Bitcrystals on Counterparty, (2) BCY (ETH) = Bitcrystals on Ethereum, or (3) BCYM (BCY Klaytn) = Bitcrystals on Klaytn chain, compatible with the First Oasis wallet where the cards blockchainized through Spells of Genesis are stored. The ones used to pay the withdraw of these cards on other chains.”).

60. RARE PEPE DIRECTORY, <http://rarepepedirectory.com> [<https://perma.cc/B5A8-MBA4>] (last visited Mar. 14, 2023).

61. Portion’s Founder, Jason Rosenstein, along with Louis Parker, ran the first live Rare Pepe auction which was held at the inaugural Rare Digital Art Festival. CryptoArt was born with the Rare Pepe Wallet, and it was the first time that creators around the world could submit and sell their own artwork. It was also the first time that digital art could have intrinsic value. RARE DIGITAL ART FESTIVAL, <https://raredigitalartfestival.splashtat.com> [<https://perma.cc/G4NH-CR87>] (last visited Mar. 14, 2023).

*B. The Proverbial Westward Expansion: NFTs Go Mainstream (2017–2020)*

In 2017, the big shift to the Ethereum blockchain was backed up by the introduction of a set of token standards, allowing the creation of tokens by developers. Building on the popularity of the *Rare Pepe* directory, creative technologists John Watkinson and Matt Hall, founders of Larva Labs,<sup>62</sup> fashioned their own series of NFTs on the Ethereum blockchain which they branded as *CryptoPunks*.<sup>63</sup> This experimental project, limited to 10,000 pieces with no two characters the same, was inspired by London punk culture and the cyberpunk movement. The *CryptoPunks* project is a hybrid between the “ERC20”<sup>64</sup> and “ERC721”<sup>65</sup> token standards. The former allows tokens to interact with each other, despite not being able to create unique tokens, while the latter has become the token standard for the current crypto art movement.<sup>66</sup>

Also in 2017, *CryptoKitties* NFTs, created by a Vancouver-based company called Axiom Zen, hit the ground running using ERC721.<sup>67</sup> *CryptoKitties* is a blockchain-based virtual game that allows players to

62. LARVA LABS, <https://larvalabs.com> [<https://perma.cc/KX92-U7R9>] (last visited Mar. 14, 2023).

63. Cryptopunks are a set of 10,000 unique characters on the Ethereum blockchain, whereby no two were the same. *Cryptopunks*, LARVA LABS, <https://larvalabs.com/cryptopunks> [<https://perma.cc/643X-N7M7>] (last visited Mar. 14, 2023).

64. Nathan Reiff, *What Are ERC-20 Tokens on the Ethereum Network?*, INVESTOPEDIA (Feb. 4, 2023), <https://www.investopedia.com/news/what-erc20-and-what-does-it-mean-ethereum/#:~:text=ERC%2D20%20allows%20developers%20to,itself%20but%20can%20be%20transferred> [<https://perma.cc/9FTF-H9RE>] (explaining that ERC-20 are fungible tokens built on Ethereum. Each token is indistinguishable from another of its kind in terms of value and characteristics. Think of it like a one-dollar bill).

65. See *ERC721 Tokens (Non-Fungible Tokens) Explained*, DISTRICT0X EDUCATIONAL PORTAL, <https://education.district0x.io/general-topics/understanding-ethereum/erc-721-tokens/> [<https://perma.cc/8VMF-J2L3>] (last visited Mar. 14, 2023). ERC-721 are standard protocol for issuing NFTs. “ERC721 is important for a number of reasons, particularly because of the new use cases it enables as well as its ability to be easily integrated into ecosystem infrastructure.” *Id.*

66. For more on the different ERC standards: ERC20, ERC721, and ERC1155, see Moussa Mazouzi, *The History of NFTs & How They Got Started*, LINKEDIN (Jan. 8, 2022), <https://www.linkedin.com/pulse/history-nfts-how-got-started-moussa-mazouzi/> [<https://perma.cc/YL89-W83A>].

67. Tonya M. Evans, *Cryptokitties, Cryptography, and Copyright*, 47 AIPLA Q.J. 219, 238 (2019) (“Cryptokitties became all the rage—and virtually crippled the Ethereum Network—at the end of 2017 . . . Each cryptokitty, unlike a dollar, apple, or the proverbial widget, is unique and, therefore, non-fungible.”).

adopt, breed, and trade virtual cats, storing them in crypto wallets.<sup>68</sup> They exploded into popularity after a single “CryptoKitty” sold for \$390,000,<sup>69</sup> landing features on major news stations and earning funding from top investors due to them generating unbelievable profits.<sup>70</sup>

Following the huge success of *CryptoKitties*, NFT gaming began to gain momentum and gather increasingly more public attention. NFT gaming and “Metaverse”<sup>71</sup> projects were in the spotlight and the first to break ground in this space was Decentraland, a decentralized VR platform on the Ethereum blockchain.<sup>72</sup> Decentraland is a *Minecraft*-like open-world gaming platform that allows players to explore, play games, build, collect items, and more, and everything that you find, earn, and build there, you own on the blockchain. Its initial coin offering (ICO) raked in a massive \$26 million in just half a minute.<sup>73</sup>

By 2018, what was once a seemingly underground movement in the crypto community had slowly transitioned into mainstream art. As an illustration, artist Kevin Abosch partnered with GIFTO for a charitable auction on Valentine’s Day of 2018.<sup>74</sup> The partnership led to a \$1 million transaction of a beautiful piece of crypto art called *The Forever Rose*.<sup>75</sup> Between 2018 and 2021, NFTs began moving into public awareness before exploding into mainstream adoption in early 2021.

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68. *Id.*

69. *10 Most Expensive NFTs, Hundreds of Thousands for a Crypto Kitty?*, MEDIUM (Dec. 18, 2020), <https://medium.com/dapp-com/10-most-expensive-nfts-hundreds-of-thousands-for-a-crypto-kitty-b152a7983036> [<https://perma.cc/NG9X-FTDT>].

70. Neer Varshney, *Someone Paid \$170,000 for the Most Expensive CryptoKitty Ever*, NEXT WEB (Sept. 5, 2018), <https://thenextweb.com/hardfork/2018/09/05/most-expensive-cryptokitty/> [<https://perma.cc/C63Z-CJWA>] (reporting that one CryptoKitty named Dragon sold for approximately \$170,000 and noting, “there can be only speculations on what makes [Dragon] so precious. Perhaps the buyer and seller wanted to make a transaction anyway, so they traded this CryptoKitty? Some speculate it could be money laundering.”).

71. Matt O’Brien & Kelvin Chan, *EXPLAINER: What is the metaverse and how will it work?*, ABC NEWS (Oct. 28, 2021), <https://web.archive.org/web/20211204012219/https://abcnews.go.com/Business/wireStory/explainer-metaverse-work-80842516>.

72. DECENTRALAND, <https://decentraland.org> [<https://perma.cc/EEE6-P8ER>] (last visited Mar. 14, 2023).

73. Stan Higgins, *\$26 Million: Blockchain VR Project Decentraland Raises New Funding in ICO*, COINDESK (Sept. 13, 2021), <https://www.coindesk.com/markets/2017/08/18/26-million-blockchain-vr-project-decentraland-raises-new-funding-in-ico/> [<https://perma.cc/EW7A-MQTH>].

74. THE FOREVER ROSE, <http://www.foreverrose.io/#/> [<https://perma.cc/3G3K-HRDR>] (last visited Mar. 14, 2023).

75. *Id.*

*C. The Present: The Year of The NFT Goldrush (2021–Present)*

In 2021, not only was there a huge explosion and surge in NFT supply and demand, but NFT also became 2021’s “Word of the Year.”<sup>76</sup> One of the biggest factors in this boom was the huge change that occurred within the art market and the industry at large when prestigious auction houses—Christie’s and Sotheby’s, namely—took their auctions into the online world and began selling NFT art. In March 2021, major rock band Kings of Leon announced that they were becoming the first band in history to release its album, *When You See Yourself*,<sup>77</sup> as an NFT.<sup>78</sup> This phenomenon arguably led to Facebook rebranding as Meta and moving into the Metaverse.<sup>79</sup> The surge in NFT demand, especially within the metaverse, has been remarkable. Ultimately, the NFT market is more efficient and more liquid than ever before and there are plenty of opportunities for new players to grab a healthy piece of the NFT Gold Rush.

IV. INTELLECTUAL PROPERTY CONSIDERATIONS OF NFT TRANSACTIONS

*A. Copyright Law*

NFTs do not change the operation of copyright law. As a default, the copyrights in a work initially vest in the author.<sup>80</sup> Copyright holders are entitled to determine the conditions under which their works will be used, copied, displayed, and even sublicensed.<sup>81</sup> Courts have decided that

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76. Collins Dictionary has chosen “NFT” as its “Word of the Year” after surging interest in the digital tokens brought it into the mainstream. *‘NFT’ Named ‘Word of the Year’ for 2021*, VOA NEWS (Nov. 24, 2021), <https://www.voanews.com/a/nft-named-word-of-the-year-for-2021/6326462.html> [<https://perma.cc/8BRP-AUQR>].

77. KINGS OF LEON, *WHEN YOU SEE YOURSELF* (RCA Records 2021).

78. Samantha Hissong, *Kings of Leon Will Be the First Band to Release an Album as an NFT*, ROLLING STONE (Mar. 3, 2021), <https://www.rollingstone.com/pro/news/kings-of-leon-when-you-see-yourself-album-nft-crypto-1135192/> [<https://perma.cc/9S7J-CE6H>].

79. *Introducing Meta: A Social Technology Company*, META (Oct. 28, 2021), <https://about.fb.com/news/2021/10/facebook-company-is-now-meta/> [<https://perma.cc/T5L9-JEHV>].

80. 17 U.S.C. § 102(a). Copyright rights, including ownership, vest automatically the moment an author creates an original work of authorship fixed in any tangible medium of expression. *Id.*

81. 17 U.S.C. § 106 (“Owning a copyright means you own a bundle of six exclusive rights: to reproduce the copyrighted work in copies; to prepare derivative works based upon the copyrighted work; to distribute copies of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending; to display the copyrighted work publicly in the case of literary, musical, dramatic, and choreographic works, pantomimes, and other audiovisual works; and to perform the copyrighted work publicly by means of a

copyrights to underlying assets do not automatically transfer.<sup>82</sup> That said, copyright transfers or assignments must be expressly established in writing.<sup>83</sup> Indeed, buyer-licensees of NFTs should conduct their due diligence to ensure that the seller-licensor of an NFT can properly assign or transfer the rights required to market, mint, and monetize the NFT.<sup>84</sup>

### 1. Buyers Beware: Does the Seller Own and Hold the Copyright?

One of the first federal lawsuits addressing NFTs involved a dispute over the copyrights in one of hip-hop's highly regarded rap albums: *Reasonable Doubt*.<sup>85</sup> In *Roc-A-Fella Records, Inc. v. Damon Dash and GoDigital Records, LLC*,<sup>86</sup> Roc-A-Fella Records, Inc. (Roc-A-Fella) sued Damon Dash (Dame), who co-founded Roc-A-Fella with Shawn Carter (Jay-Z) and Kareem Burke, in the United States District Court for the Southern District of New York after Dame revealed his plan to mint and sell an NFT of the copyright to Jay-Z's platinum-certified debut album.<sup>87</sup>

This lawsuit arose when Dame used SuperFarm, “an electronic platform that allows people to create, farm, buy, sell, auction, and swap NFTs,” to announce an auction of an NFT bearing the copyrights to *Reasonable Doubt* on the Ethereum blockchain.<sup>88</sup> Roc-A-Fella responded

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digital audio transmission in the case of sound recordings. Each of the rights can be separately licensed. Each of the rights can be subdivided and licensed to more than one licensee.”).

82. See e.g., *Radio Television Espanola S.A. v. New World Ent., Ltd.*, 183 F.3d 922, 927 (9th Cir. 1999) (holding that the parties' intent, as evidenced by the writing, must demonstrate a transfer of the copyright).

83. 17 U.S.C. § 204(a). The Copyright Act provides that “[a] transfer of copyright ownership, other than by operation of law, is not valid unless an instrument of conveyance, or a note or memorandum of the transfer, is in writing and signed by the owner of the rights conveyed . . .” *Id.*

84. Peter Willsey et al., *NFT litigation: Shaping IP rights in the metaverse*, 40 WESTLAW J. COMPUT. & INTERNET (2022).

85. JAY-Z, REASONABLE DOUBT (Priority Records 1996).

86. No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. Jun. 18, 2021).

87. Complaint, *Roc-A-Fella Recs. Inc. v. Damon Dash*, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. Jun. 18, 2021).

88. *Id.* at 6–7, ¶¶ 23–24. In an announcement on the website, Superfarm touted the uniqueness of the planned sale: “Selling the copyright to Jay-Z's Reasonable Doubt as an NFT is a groundbreaking landmark—both for the crypto space and the broader music industry. The newly minted NFT will prove ownership of the album's copyright, transferring the rights to all future revenue generated by the album from Damon Dash to the auction winner.” *Id.*

to this announcement by sending cease-and-desist letters to SuperFarm and Dame, which resulted in the auction being canceled.<sup>89</sup> On June 18, 2021, before another platform had the opportunity to host the NFT auction, Roc-A-Fella sued Dame.<sup>90</sup> In its complaint, Roc-A-Fella alleged and sought: (1) a judgment declaring Roc-A-Fella as the owner of all rights, including all copyrights, to *Reasonable Doubt*, (2) damages for unjust enrichment, conversion, replevin, and breach of fiduciary duty; and, (3) an injunction to enjoin Dame from selling any interest in *Reasonable Doubt*.<sup>91</sup> On July 2, 2021, U.S. District Judge John P. Cronan issued a temporary restraining order against Dame until the final resolution of the action.<sup>92</sup>

On July 16, 2021, Dame filed his answer to Roc-A-Fella's complaint, arguing that "there is nothing in our agreement between us that prohibits me or Jay-Z from selling our share of Roc A Fella Records, Inc., the company which owns Reasonable Doubt."<sup>93</sup> Dame conceded that he did not own *Reasonable Doubt*, however, he claimed that he was opportunistically and lawfully using the NFT market to auction a digital representation of his one-third interest in Roc-A-Fella itself.<sup>94</sup> Though it was later denied by the court, Dame also ambitiously sought a temporary restraining order to enjoin Roc-A-Fella from holding its July 16 shareholder meeting.<sup>95</sup>

Further clouding the issue, on August 6, Roc-A-Fella filed an amended complaint after Dame entered into an agreement with GoDigital Media

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89. Complaint at 36, *Roc-A-Fella Recs. Inc. v. Damon Dash*, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. Jun. 18, 2021).

90. *Id.* at 7, 27.

91. *Id.* at 8–10, ¶¶ 28–45, 53–56.

92. Order, *Roc-A-Fella Records Inc. v. Damon Dash*, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. June 27, 2021).

93. Answer, *Roc-A-Fella Records Inc. v. Damon Dash*, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. July 16, 2021); Murray Stassen, *Damon Dash Insists He's Entitled To Sell Share of Jay-Z's Reasonable Doubt As NFT—Despite Being Sued By Roc-A-Fella Records*, MUSIC BUS. WORLDWIDE (June 22, 2021), <https://www.musicbusinessworldwide.com/damon-dash-insists-hes-entitled-to-sell-share-of-jay-zs-reasonable-doubt-as-nft-despite-being-sued-over-plan/> [https://perma.cc/V65P-2YHP].

94. Answer at 1, *Roc-A-Fella Records Inc. v. Damon Dash*, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. July 16, 2021).

95. Memorandum of Law in Support of Plaintiff's Ord. to Show Cause to Enjoin Meeting of S'holders Scheduled for July 16, 2021 at 5:00PM EST, *Roc-A-Fella Records Inc. v. Damon Dash*, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. July 16, 2021).

Group (GDMG),<sup>96</sup> granting the right to license *Reasonable Doubt* NFTs to websites, naming GDMG as a co-defendant.<sup>97</sup> On September 8, Dame and GDMG answered the Amended Complaint and counterclaimed for a declaratory judgment that its agreement with Dame was valid.<sup>98</sup> After considering the pleadings and Joint Stipulations made on June 13, 2022, Judge Cronan issued an order, declaring:

As between the Parties, [Roc-A-Fella], Inc. owns all rights to the album Reasonable Doubt, including its copyright, and this Judgment shall prohibit the altering in any way, sale, assignment, pledging, encumbering, contracting with regard to, or in any way disposing of [Roc-A-Fella]'s property interest in Reasonable Doubt, including its copyright, and including through any means such as auctioning a non-fungible token reflecting, referring, or directing to such interest, unless duly authorized by [Roc-A-Fella]; provided, however, that nothing in this Judgment shall prevent [Dame] from selling, assigning, pledging, encumbering, contracting with regard to, or in any way disposing of his one-third (1/3rd) ownership interest in [Roc-A-Fella].<sup>99</sup>

Not only does the judgment establish that Roc-A-Fella owns all rights to *Reasonable Doubt*, but it also prohibits any Roc-A-Fella member, like Dame, or shareholder from auctioning as an NFT any interest in *Reasonable Doubt*.<sup>100</sup> However, this judgment does offer a glimmer of hope for future buyers: neither Dame nor other joint copyright owners,<sup>101</sup> are prohibited from transferring or assigning their interest, including presumably through an NFT.

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96. GODIGITAL MEDIAL GROUP, <https://godigitalmg.com> [<https://perma.cc/XWS4-ZKM3>] (last visited Mar. 14, 2023). GDMG is a privately held multi-national conglomerate.

97. First Amended Complaint, Roc-A-Fella Records Inc. v. Damon Dash, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. Aug. 6, 2021).

98. Answer of First Amended Complaint, Roc-A-Fella Records Inc. v. Damon Dash, No. 1:21-CV-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. Sep. 8, 2021).

99. Final Judgment, Roc-A-Fella Records Inc. v. Damon Dash, No. 1:21-cv-05411, 2022 U.S. Dist. LEXIS 114591 (S.D.N.Y. Jun. 27, 2022).

100. *Id.*

101. Generally, co-owners of copyrights may exploit and license jointly owned works independently, without the consent of the other co-owners, subject to the obligation to account to all other co-owners for an equitable share of the profits received. James K. Rothstein, *Unilateral Settlements and Retroactive Transfer: A Problem of Copyright Co-Ownership*, 157 U. PA. L. REV. 881, 885 (2009).



## 2. Are “Pre-NFT” Contracts Sufficiently Forward-Looking to Protect Preexisting Copyrighted Works?

Copyright ownership can cause significant issues when not sufficiently defined in an NFT licensing agreement. This issue is only compounded when considering “pre-NFT” contracts, or any agreement between parties that was contemplated before the advent of NFTs. Films that are universal favorites and that hold up after being rescreened repeatedly are labeled “classics.” Classics films—such as *The Wizard of Oz*,<sup>102</sup> *Gone with the Wind*,<sup>103</sup> and *The Godfather*<sup>104</sup>—are five-starred, renowned reference points in film mythology that have become interwoven into American cultural folklore. As NFT law emerges, there is a frontier question in the entertainment industry of whether pre-NFT contractual provisions prohibit minting NFTs related to preexisting films or television series.

The case of *Miramax, LLC v. Quentin Tarantino, VisionA Romantica, Inc.*,<sup>105</sup> presents a classic example of Web2 copyright laws being applied in a Web3 environment. The suit addressed the issue of whether the original 1993 contract between acclaimed filmmaker, Quentin Tarantino (Tarantino), and the Hollywood film distributor, Miramax, contemplated Miramax’s right to mint NFTs or whether Tarantino’s reservation of rights in the transaction encompassed this.<sup>106</sup>

The case arose in November 2021, when Tarantino, and his company Visiona Romantica, announced his plan to sell seven “Secret NFTs” based on his original handwritten script of the 1994 film *Pulp Fiction* on the OpenSea platform, including “exclusive custom commentary” from “uncut first handwritten scripts” from the film, as well as unique iconic props from other Tarantino films.<sup>107</sup> On November 11, 2021, a Twitter account named “@TarantinoNFTs” announced that the sale of the NFTs would occur in December 2021.<sup>108</sup> For reference, in January of 2022, the

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102. THE WIZARD OF OZ (Metro-Goldwyn-Mayer 1939).

103. GONE WITH THE WIND (Selznick International Pictures 1939).

104. THE GODFATHER (Paramount Pictures 1972).

105. 2:21-cv-08979, (C.D. Cal. Nov. 16, 2021).

106. *Id.* at \*1.

107. *Quentin Tarantino Revealed as Iconic Artist Behind First-Ever Secret NFTs, Showcasing Never-Before-Seen Work Revealed Only to NFT Owner*, GLOBENEWSWIRE (Nov. 2, 2021), <https://www.globenewswire.com/news-release/2021/11/02/2325448/0/en/Quentin-Tarantino-Revealed-as-Iconic-Artist-Behind-First-Ever-Secret-NFTs-Showcasing-Never-Before-Seen-Work-Revealed-Only-to-NFT-Owner.html> [https://perma.cc/Q9LM-H7GG].

108. Complaint at 14, ¶ 47, *Miramax LLC v. Tarantino*, 2:21-cv-08979 (C.D. Cal. Nov. 16, 2021).

first NFT collectible from Tarantino's collection, "Royale with Cheese," was purchased by Secret Network for \$1.1 million.<sup>109</sup>

On November 16, 2021, Miramax filed a lawsuit in the United States District Court for the Central District of California, alleging breach of contract, trademark infringement, and copyright infringement.<sup>110</sup> According to the complaint, Tarantino directly infringed on Miramax's exclusive rights in *Pulp Fiction* because minting NFTs were unauthorized derivative works.<sup>111</sup> Miramax contended that the right to create NFTs was contemplated in forward-looking contractual language.<sup>112</sup> In the agreement, Miramax acquired "all rights . . . now or hereafter known . . . in all media now or hereafter known," while Tarantino reserved certain limited rights, including "print publication" and "interactive media."<sup>113</sup> According to Miramax, the sale of the NFTs exceeded Tarantino's "narrow" reserved rights and was thus a breach of contract.<sup>114</sup>

On December 9, 2021, Tarantino filed an answer,<sup>115</sup> denying many of Miramax's allegations and asserting several affirmative defenses, including that the NFTs fell under the fair use exception to the Copyright Act.<sup>116</sup> Tarantino also asserted that the publication of NFTs was within his reserved publishing rights and therefore he may develop, market, and sell the *Pulp Fiction* NFTs.<sup>117</sup>

On September 8, 2022, Tarantino and Miramax LLC settled their disputes without disclosing terms.<sup>118</sup> This leaves the issue of whether pre-NFT contracts, which do not explicitly mention NFTs, can be forward-looking enough to prohibit minting NFTs of pre-existing works unsettled. Still, this settlement should encourage parties to negotiate

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109. Nick Karoglou, *SCRT Labs Announces Triumphant Sale of First Never-Before-Seen-Or-Heard Tarantino NFT for \$1.1 Million*, BUSINESS WIRE (Jan. 24, 2022), <http://www.businesswire.com/news/home/20220121005513/en/SCRT-Labs-Announces-Triumphant-Sale-of-First-Never-Before-Seen-Or-Heard-Tarantino-NFT-for-1.1-Million>.

110. Complaint at 3–4, ¶ 15–19, *Miramax LLC v. Tarantino*, 2:21-cv-08979 (C.D. Cal. Nov. 16, 2021).

111. *Id.* at 17, ¶ 56.

112. *Id.* at 5, ¶ 22.

113. *Id.* at 4–5, ¶¶ 20–21.

114. *Id.* at 15–16, ¶¶ 52–53.

115. Answer, *Miramax LLC v. Tarantino*, 2:21-cv-08979 (C.D. Cal. Nov. 16, 2021).

116. *Id.* at 15.

117. *Id.* at 12.

118. Notice of Settlement, *Miramax LLC v. Tarantino*, 2:21-cv-08979 (C.D. Cal. Sept. 8, 2022).

before launching NFTs to avoid costly litigation. Moreover, that both parties presented meritorious arguments which resulted in a settlement suggests that there is relatively equal bargaining power between the parties.

### 3. What About the A.I. Elephant in the Room?: The Generative Art Issue

Generative art is an expression that has emerged as an attractive sub-sector within the crypto art space.<sup>119</sup> Generative art describes algorithmic art that is created programmatically, via smart contracts, by artists through artificial intelligence (AI).<sup>120</sup> Although generative art features a collaboration between man and machine, AI operates autonomously by using its own generative process to produce original artwork. For instance, Robbie Barrat, a self-taught AI prodigy, uses neural networks that consist of algorithms called a generator and a discriminator to create AI art.<sup>121</sup> As a seventeen-year-old, Barrat developed an AI program that could write its own raps, complete with semi-appropriate pauses, using 6,000 lines from the iconic and enigmatic artist Kanye West.<sup>122</sup>

Traditional copyright law fragments the scope of copyrights subsisting in AI-assisted work generated by AI artists like Barrat. The U.S. Copyright Review Board ruled that a work autonomously created entirely by a computer algorithm running on a machine cannot be

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119. Mason Marcobello, *What Are Generative Art NFTs?*, COIN DESK (Oct. 25, 2022), <https://www.coindesk.com/learn/what-are-generative-art-nfts/> [https://perma.cc/27WB-2AT7].

120. Jane Ginsburg & Luke Ali Budiardjo, *Authors And Machines*, 34 BERKELEY TECH. L.J. 343, 348 (2019) (“The burgeoning of computer-enabled works—outputs of generative machines designed to create works and to mimic human creativity, perhaps through the use of ‘artificial intelligence’ techniques like machine learning—offers the newest iteration of [copyright] challenges.”); Ryan Calo, *Artificial Intelligence Policy: A Primer and Roadmap*, 51 U.C. DAVIS L. REV. 399, 404–05 (2017) (“The term ‘artificial intelligence’ is an ‘umbrella term,’ comprising ‘many different techniques,’ and broadly refers to the ‘set of techniques aimed at approximating some aspect of human or animal cognition using machines.’”).

121. Joe Dworetzky, *Q&A: Robbie Barrat on training neural networks to create art*, THE STANFORD DAILY (June 12, 2018), <https://stanforddaily.com/2018/06/12/qa-robbie-barrat-on-training-neural-networks-to-create-art/> [https://perma.cc/L84K-PTES].

122. Dave Gershgorn, *A West Virginia teen taught himself how to build a rapping AI using Kanye West lyrics*, QUARTZ (July 20, 2022), <https://qz.com/920091/a-west-virginia-teen-taught-himself-how-to-build-a-rapping-ai-using-kanye-west-lyrics/> [https://perma.cc/32HS-HFPB].

protected by copyright laws.<sup>123</sup> According to the Copyright Office, copyright only protects the fruits of intellectual labor that are “founded in the creative powers of the [human] mind.”<sup>124</sup>

This falls in line with existing U.S. law where the author must be human for copyrights to subsist. In the widely publicized “Monkey Selfie” case, *Naruto v. Slater*,<sup>125</sup> the United States Court of Appeals for the Ninth Circuit recognized that only a human can create art that has a copyright.<sup>126</sup> In this case, a crested macaque, named Naruto, picked up photographer David Slater’s camera and clicked photographs of himself. The photographer published the “Monkey Selfies” in a book and claimed copyright ownership of the photographs. At the same time, People for Ethical Treatment of Animals (PETA) intervened as Next Friends on behalf of Naruto, claiming that Naruto owned the copyright to the photographs. Ultimately, Naruto’s claim was dismissed because of a lack of standing under the Copyright Act because only humans can create copyrightable art.<sup>127</sup>

Thus, it appears that Barrat’s rapping robot cannot be an author that owns copyrights, but it does not foreclose AI artists like Barrat from claiming some degree of authorship in the resulting work. Some other countries, like the United Kingdom, protect such works by granting copyright protection to the person that directs the computer to generate the work.

### B. Trademark Law

A trademark is a word, symbol, or phrase used to identify a particular manufacturer or seller’s products and distinguish them from the products of another.<sup>128</sup> Trademarks make it easier for consumers to

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123. *Re: Second Request for Reconsideration for Refusal to Register A Recent Entrance to Paradise (Correspondence ID 1-3ZPC6C3; SR # 1-7100387071)*, COPYRIGHT REVIEW BOARD (Feb. 14, 2022), <https://www.copyright.gov/rulings-filings/review-board/docs/a-recent-entrance-to-paradise.pdf> [<https://perma.cc/B6L2-FUBX>].

124. COMPENDIUM OF U.S. COPYRIGHT OFFICE PRACTICES § 306 (3d ed. 2021) (quoting *In Re Trade-Mark Cases*, 100 U.S. 82, 94 (1879)); *see also* COMPENDIUM OF U.S. COPYRIGHT OFFICE PRACTICES § 313.2 (3d ed. 2021) (noting that the Office will not register works “produced by a machine or mere mechanical process” that operates “without any creative input or intervention from a human author” because, under the statute, “a work must be created by a human being.”).

125. 888 F.3d 418 (9th Cir. 2018).

126. *Id.* at 426.

127. *Id.*

128. 15 U.S.C. § 1127.

quickly identify the source of a given good. For example, the brand identifier “Coca-Cola” distinguishes the brown-colored soda of one manufacturer from the brown-colored soda of another, like Pepsi. Trademarks do not expire after a set period, persisting indefinitely so long as the trademark owners continue to use the mark in commerce.<sup>129</sup> The Lanham Act ensures this by providing that registration is not subject to cancellation where a mark is used by a related company, so long as the controller exercises “quality control”<sup>130</sup> concerning the nature and quality of goods being proffered for a license.<sup>131</sup> Thus, seller-licensors of NFTs bearing their brands must exercise control over the nature and quality of their digital assets to avoid customer confusion or, more importantly, counterfeiting.

Accordingly, counterfeit products and trademark infringement of NFTs present another legal risk related to buying and selling these unique digital assets. The investment potential combined with the immense popularity of NFTs has resulted in increased incidents of cyber fraud in the market.<sup>132</sup> Counterfeiters defraud consumers by selling bogus NFTs, devoid of any intellectual property (IP) rights, on fake marketplaces by using their site branding, content, and legal documentation to appear authentic. While platforms like MarqVision,<sup>133</sup> an AI-powered IP protection service, detect and flag NFT fakes and counterfeits, NFT trademark infringement remains a prevalent issue.

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129. *See, e.g.*, *Dawn Donut Co. v. Hart’s Food Stores, Inc.*, 267 F.2d 358 (2d Cir. 1959) (holding that the absence of a written contract right to inspect and control a licensee’s use of a mark does not preclude a finding that the trademark owner met his duty of control, so long as other evidence exists to show that the owner exercised “sufficient” control). Sufficient control may be direct control (such as supplying or inspecting facilities, products, process, etc.), reliance control (such as relying on the licensee or another agent), or actual control (such as no written provision, but licensor demonstrates actual control).

130. *Id.*

131. 15 U.S.C. § 1051.

132. Dorian Batycka, *Counterfeit NFTs are creating major problems for digital platforms—but new tools to spot fakes are on the rise*, THE ART NEWSPAPER (Apr. 1, 2022), <https://www.theartnewspaper.com/2022/04/01/how-counterfeit-create-problems-for-nft-platforms> [<https://perma.cc/Q99S-J9D8>].

133. MARQVISION, <https://www.marqvision.com> [<https://perma.cc/DYY2-KYJM>] (last visited on Mar. 14, 2023).

### 1. Trademark Infringement in the World of NFTs

Coined the “Sneaker Wars,”<sup>134</sup> a metaverse battle royale arose between Nike and StockX, an online sneaker resale platform, after StockX used Nike’s famous swoosh marks in connection with StockX’s entry into the NFT market. This matter could have far-reaching implications for how an NFT is defined and whether incorporating branded images on NFTs in the resale market would be considered trademark infringement.

On February 3, 2022, Nike swooshed in and filed a lawsuit against the resale giant StockX in the United States District Court for the Southern District of New York.<sup>135</sup> In their suit, Nike alleged trademark infringement, dilution, and unfair competition against StockX after StockX sold NFTs linked to trademarks, digital images, and physical versions of Nike sneakers, called “Vault NFTs.”<sup>136</sup> Nike alleged that StockX sold upward of 550 Nike-branded NFTs and has “recogniz[ed] the tremendous value of the Nike brand to consumers.”<sup>137</sup> For example, at the time of the complaint, the physical pair of Nike’s 2022 Nike Dunk Low, “Retro White Black Color Wave,” retailed for \$100 on Nike’s website whereas the average resale price of the StockX’s 2021 version of the sneaker retailed for \$282 on StockX’s website.<sup>138</sup> Yet, during that same span, the average price of the Vault NFT linked to those shoes as of the same date was \$809, with the highest trade being \$3,500.<sup>139</sup> “StockX’s Vault NFTs are not Nike products;” rather, they are “virtual products” traded for inflated prices higher than both the original retail price and the current resale price on the secondary market.<sup>140</sup>

On March 31, 2022, StockX filed its answer,<sup>141</sup> stating that Vault NFTs on their platform are “*absolutely not* ‘virtual products’ or digital sneakers; instead, each Vault NFT is ‘tied [to] a specific physical good that has

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134. Andrew Rossow, *The Nike v. StockX Lawsuit Could Determine What Type of NFTs Can Be Created*, NFT NOW (May 26, 2022), <https://nftnow.com/features/the-nike-v-stockx-lawsuit-could-determine-what-type-of-nfts-can-be-created/> [<https://perma.cc/HFR7-GDR2>].

135. Complaint, Nike, Inc. v. StockX LLC, 1:22-CV-00983, 2023 U.S. Dist. LEXIS 4516 (S.D.N.Y. Feb. 3, 2022).

136. *Id.* at 3, ¶ 5.

137. *Id.* at 29, ¶ 64.

138. *Id.* at 16–17, ¶ 46.

139. *Id.* at 18.

140. *Id.* at 34–35, ¶¶ 73–76.

141. Answer, Nike, Inc. v. StockX LLC, 1:22-CV-00983, 2023 U.S. Dist. LEXIS 4516 (S.D.N.Y. Mar. 31, 2022).

already been authenticated[.]”<sup>142</sup> According to StockX, not only do the Vault NFTs have no intrinsic value, but each is “effectively a claim ticket, or a ‘key’ to the underlying Stored Item.”<sup>143</sup> StockX defended its use as “normative fair use . . . no different than major e-commerce retailers and marketplaces who use images and descriptions of products to sell physical sneakers and other goods, which consumers see (and are not confused by) every single day.”<sup>144</sup> Further, StockX argued that its use of Nike branding and images as part of its display and sale of Vault NFTs was proper under, among several affirmative defenses, the first sale doctrine.<sup>145</sup>

The price disparity between Nike’s retail price of its Nike Dunk Low sneaker and its associated NFT on StockX’s platform suggests there is confusion about whether Vault NFTs were separate assets with a value distinct from their physical asset counterparts<sup>146</sup> or merely a receipt that simply authenticates and demonstrates ownership of physical sneakers.<sup>147</sup> This case will be pivotal in laying the legal groundwork for how courts will interpret trademark rights in connection with the creation, purchase, and sale of NFTs.

## 2. Artistic Expressions of Luxury Brands or Real-World Art

Modern artists and designers often create art based on their interpretations of the world around them. Minting NFTs as a work of visual art could raise trademark infringement concerns. As a case in point, on January 14, 2022, French fashion house Hermès International and the Hermès of Paris, Inc., sued Mason Rothschild, a digital artist, in the United States District Court for the Southern District of New York for trademark infringement, false designation of origin, trademark dilution, cybersquatting, and injury to business reputation and dilution.<sup>148</sup> This was in response to Rothschild’s release of *MetaBirkins*,

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142. *Id.* at 3 (emphasis in original).

143. *Id.*

144. *Id.* at 8.

145. *Id.* at 2. Under the first sale doctrine, the right of the trademark owner to control product distribution does not extend beyond the first sale of the product, allowing the trademarked product to be resold without the fear of the trademark owner bringing a lawsuit against them. 17 U.S.C. § 109(a).

146. Complaint at 3, ¶ 5, Nike, Inc. v. StockX LLC, 1:22-CV-00983, 2023 U.S. Dist. LEXIS 4516 (S.D.N.Y. Feb. 3, 2022).

147. Answer at 8, Nike, Inc. v. StockX LLC, 1:22-CV-00983, 2023 U.S. Dist. LEXIS 4516 (S.D.N.Y. Mar. 31, 2022).

148. Complaint, Hermès International, et al. v. Mason Rothschild, 1:22-CV-00384, 2022 U.S. Dist. LEXIS 89799 (S.D.N.Y. Jan. 14, 2022).

a collection of 100 NFTs linked to digital images of Hermès Birkin bags covered in faux fur in a range of colors and designs.<sup>149</sup> Hermès claimed that unauthorized use of its trademark is Rothschild’s “ruse” to get rich quick from its famous Hermès Birkin trademark because it is a “highly valuable asset in the physical world.”<sup>150</sup>

On February 9, Rothschild filed a motion to dismiss the complaint, asserting a fair use defense under the First Amendment.<sup>151</sup> To support his argument, Rothschild claimed that his *MetaBirkins* NFT is merely selling an “expression” of the Hermès Birkin bag as a form of commercial speech. Rothschild relied heavily on the *Rogers* test, adopted in *Rogers v. Grimaldi*.<sup>152</sup> The *Rogers* test seeks to balance the public interest in free speech against the protection of the rights of trademark owners by providing that use of a trademark in an artistic or expressive work is actionable, under the Lanham Act, only if the use of the mark (1) has no artistic relevance to the underlying work, or (2) is explicitly misleading as to the source or content of that work.<sup>153</sup>

Rothschild argued that the use of *MetaBirkins* met both prongs of the *Rogers* test.<sup>154</sup> First, the use of the Hermès Birkin mark is artistically relevant because they “invite viewers to consider the difference between the material objects—made of animal skins in reality—and the fantasized, immaterial images with their faux fur.”<sup>155</sup> Therefore, Rothschild claimed that it was not “attacking the Birkin, but inviting consideration of its meaning as an image, rather than as a handbag.”<sup>156</sup> Second, Rothschild contended that the use of the *MetaBirkins* name in its website and social media accounts is not explicitly misleading because his art project clearly identified the “partnership with Basic.Space (not Hermès).”<sup>157</sup>

United States District Judge Jed S. Rakoff, writing for the United States District Court for the Southern District of New York, partially

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149. *Id.* at 14–15, ¶ 56.

150. *Id.* at 2–3, ¶¶ 3–5.

151. Memorandum in Support of Motion to Dismiss, Hermès International, et al. v. Mason Rothschild, 1:22-CV-00384, 2022 U.S. Dist. LEXIS 89799 (S.D.N.Y. Feb. 9, 2022). *See also* 17 U.S.C. § 107.

152. 875 F.2d 994 (2d Cir. 1989).

153. *Id.* at 999.

154. Memorandum in Support of Motion to Dismiss at 8, Hermès International, et al. v. Mason Rothschild, 1:22-CV-00384, 2022 U.S. Dist. LEXIS 89799 (S.D.N.Y. Feb. 9, 2022).

155. *Id.*

156. *Id.* at 9.

157. *Id.* at 14.



agreed. The court found that the “digital images of handbags [ ] could constitute a form of artistic expression,” requiring the application of the *Rogers* test.<sup>158</sup> Further, the court reasoned that an NFT is simply code pointing to the location of a digital image for authentication akin to numbered copies of physical paintings, therefore using NFTs to authenticate an image does not render them commodities without First Amendment protection.<sup>159</sup> Nonetheless, the court denied Rothschild’s motion to dismiss because Hermes’s amended complaint contained sufficient factual allegations that the use of the *MetaBirkins* mark was not artistically relevant and could be explicitly misleading as to the source of Rothschild’s works.<sup>160</sup>

As the parties gather expert testimony and customer surveys for summary judgment proceedings, this matter will be closely watched for its potential value to current and future Web3-centric lawsuits that continue to proliferate in the current litigious NFT minefield.<sup>161</sup>

### 3. NFT Launchings Utilizing a Celebrity’s Name, Image, and Likeness

In a separate, but related, field of law, the use of a celebrity’s name, image, or likeness (NIL) on NFTs without permission may violate a person’s right of publicity, which protects against the misappropriation of a celebrity’s (or non-celebrity’s) name, likeness, or other indicia of personal identity.<sup>162</sup> Where copyright and trademark laws protect someone’s creation, the right of publicity protects someone’s persona

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158. Memorandum Order at 11, *Hermès International v. Mason Rothschild*, 1:22-CV-00384, 2022 U.S. Dist. LEXIS 89799 (S.D.N.Y. May 18, 2022).

159. *Id.* at 12.

160. *Id.* at 18.

161. Zerbo, *Hermès v. Rothschild: A Timeline of Developments in a Case Over Trademarks, NFTs*, THE FASHION LAW (Jan. 13, 2023), <https://www.thefashionlaw.com/hermes-v-rothschild-a-timeline-of-developments-in-a-case-over-trademarks-nfts/> [https://perma.cc/63SR-8WZU].

162. Mioko Tajika, *Queen’s Death Gives Birth to A Flood of NFTs and a Question About the Right of Publicity*, JD SUPRA (Sept. 28, 2022), <https://www.jdsupra.com/legalnews/queen-s-death-gives-birth-to-a-flood-of-9245451/> [https://perma.cc/TSN7-GP9Z].

itself.<sup>163</sup> For example, the case *McCollum v. Opulous*,<sup>164</sup> in the United States District Court for the Central District of California, involved a claim by Miles Parks McCollum, better known as Grammy-nominated recording artist Lil Yachty, against a UK-based NFT company, Opulous.<sup>165</sup> Lil Yachty brought claims including trademark infringement and violations of his right to privacy and publicity due to defendant Opulous's unauthorized use of his trademarked NIL in launching and offering Opulous's NFT collections to raise more than \$6.5 million in venture capital.<sup>166</sup>

According to the complaint, Opulous pitched Lil Yachty on being involved with the Opulous platform, but the parties did not reach any agreement.<sup>167</sup> Yet, on June 1, 2021, Opulous launched a press and advertisement campaign representing that Lil Yachty was affiliated with the launch of Opulous, which included offering his copyrighted musical works for sale and NFT "drops."<sup>168</sup> On August 3, the United States District Court for the Central District of California denied Opulous's motion to dismiss and determined that the foreign company was subject to the jurisdiction of U.S. courts based, in part, on its social media activity.<sup>169</sup> This finding is procedurally important, as it provides a clear warning to both domestic and international defendants that their social media activities may be highly relevant to a personal jurisdiction analysis under state long-arm legislation.<sup>170</sup>

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163. NEW YORK PRACTICE SERIES, COMMERCIAL LITIGATION IN NEW YORK STATE COURTS § 135:13 (5th ed. 2022) ("In this day and age, when many brands use social media to connect with their customers and any individual can be a social media 'influencer,' even a single post on a brand's Instagram page may implicate an individual's right of publicity, whether the subject is a public figure or not.").

164. Complaint, *McCollum v. Opulous*, 2:22-CV-00587, 2022 U.S. Dist. LEXIS 214634 (C.D. Cal. Jan. 27, 2022).

165. *Id.*

166. *Id.* at 3.

167. *Id.* at 7–8, ¶¶ 30–37.

168. A drop refers to the exact date, time, and generally the minting price of the NFT. As such, an NFT drop is the release of a non-fungible token project. Daniel Kahan, *NFTs 101: What the Heck is an NFT Drop?*, DOINGUD, <https://blog.doingud.com/nfts-101-what-the-heck-is-an-nft-drop/>.

169. Minutes (in Chambers) Order Denying Defendants' Motion to Dismiss for Lack of Personal Jurisdiction, *McCollum v. Opulous*, 2:22-CV-00587, 2022 U.S. Dist. LEXIS 214634 (C.D. Cal. Aug. 3, 2022).

170. Dyan Finguerra-DuCharme & Nicholas Saady, *United States: A Cautionary Tale On Social Media And US Jurisdiction*, LAW 360 (Aug. 19, 2022),

V. REGULATORY CONSIDERATIONS: SELLING THE SIZZLE  
WITHOUT THE STAKE

NFTs provide lucrative investment opportunities for sophisticated investors to generate streams of income or share in their underlying portfolio of investment assets.<sup>171</sup> According to the Commissioner of the Securities and Exchange Commission (SEC) Hester Peirce,<sup>172</sup> there is currently no uniform regulatory framework informing digital art creators and investors whether NFTs qualify as a regulated financial product under the laws governing its issuance and distribution as a specific kind of property in the U.S.<sup>173</sup> The SEC has mainly targeted fungible tokens, which are digital assets that are not distinguishable from one another. Currently, neither U.S. regulators nor U.S. courts have classified NFTs as “securities.”<sup>174</sup>

The Supreme Court of the United States applies the *Howey* test<sup>175</sup> to determine whether any contract, asset, transaction, or scheme is an “investment contract,” requiring compliance with federal securities regulations. An investment contract exists where there is the (1) investment of money (2) in a common enterprise (3) with a reasonable expectation of profits (4) to be derived from the efforts of others.<sup>176</sup> Analyzing these prongs depends on the facts and circumstances of the specific NFT.

While a purchase of an NFT will likely satisfy the first prong, it has been difficult for the SEC to prove the existence of a common

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<https://pryorcashman.gjassets.com/content/uploads/2022/08/A-Cautionary-Tale-On-Social-Media-And-US-Jurisdiction.pdf> [<https://perma.cc/TL9C-YGUQ>].

171. Hagen Rooke & Nina Carlina Sugianto, *Is my NFT a security?*, REED SMITH LLP (Aug. 1, 2022), <https://www.reedsmith.com/en/perspectives/metaverse/2022/08/is-my-nft-a-security> [<https://perma.cc/NSD9-G48Y>].

172. *Biography: Commissioner Hester M. Peirce*, U.S. SEC. & EXCH. COMM’N, <https://www.sec.gov/about/commissioners/hester-m-peirce> [<https://perma.cc/46ES-VUDM>] (last visited Mar. 14, 2023).

173. Stefania Palma & Patrick Temple-West, *SEC must clarify which NFTs will be regulated, says commissioner*, FINANCIAL TIMES (Oct. 17, 2022), <https://www.ft.com/content/e8df6ea4-e9fb-4058-9a36-cef9c12f4726> [<https://perma.cc/7NMN-6QTR>].

174. The term “security” means any note, stock, participation in any profit-sharing agreement, investment contract, and other investment instruments. 15 U.S.C. § 77b(a)(1).

175. The *Howey* test was laid out by the Supreme Court of the United States in *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

176. *Id.* at 298–99.

enterprise.<sup>177</sup> However, the popularity of NFT “staking”<sup>178</sup> could raise securities issues. Staking is a way for NFT owners to put their unique NFTs on the blockchain and into the marketplace by lending those digital assets to “NFT stakers” and, in return, receiving a sales percentage, royalty payment, or other benefits as determined by the smart contract.<sup>179</sup> The owners retain ownership of the NFT and reclaim possession at the end of the contracted staking period.<sup>180</sup> In these circumstances, this could satisfy the second prong, serving as proof of existence of a common scheme. As to the third prong, a court could also determine that NFT owners who engage in staking to earn passive income do so expecting to receive a profit. Further, there is a colorable argument that the fourth *Howey* prong is satisfied because NFT owners use the efforts of NFT stakers to generate passive income. In sum, unless the NFTs involved demonstrate utility and the marketing is aimed at that utility rather than the possibility of financial gain, NFT staking may be considered a securities scheme.

Similarly, brand-based collections of NFTs are being “fractionalized” to allow for divided ownership of one or more unique assets.<sup>181</sup> Fractional NFTs bring a great deal of liquidity to the NFT marketplace because smaller investors can participate as opposed to only a few deep-pocketed collectors.<sup>182</sup> In March 2021, SEC Commissioner Peirce warned NFT issuers that selling fractionalized interest in NFTs could be considered investment contracts under U.S. securities law.<sup>183</sup> To support

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177. William K. Pao et al., *Howey Should Think About NFTs and Securities Laws*, O'MELVENY & MYERS LLP (Sept. 29, 2022), <https://www.omm.com/resources/alerts-and-publications/alerts/howey-should-think-about-nfts-and-securities-laws/>.

178. Corey Barchat, *NFT staking explained*, MOON PAY (Mar. 11, 2022), <https://www.moonpay.com/nft/nft-staking> [<https://perma.cc/3TZX-GGZ7>] (“NFT staking refers to an NFT owner locking up their asset for a certain period of time, earning passive income in the form of cryptocurrency while doing so.”).

179. *Id.*

180. *Id.*

181. NFT fractionalization is simply the act of dividing the ownership of an NFT into smaller fractions. Jinia Shawdagar, *What are Fractionalized NFTs?*, CRYPTOVANTAGE (Sept. 22, 2022), <https://www.cryptovantage.com/non-fungible-tokens/what-are-fractionalized-nfts/> [<https://perma.cc/HP92-CLPT>].

182. *Id.*

183. Samuel Haig, *SEC's 'Crypto Mom' warns selling fractionalized NFTs could break the law*, COINTELEGRAPH (Mar. 26, 2021), <https://cointelegraph.com/news/sec-s-crypto-mom-warns-selling-fractionalized-nfts-could-break-the-law> [<https://perma.cc/A25T-SCNB>] (“You better be careful that you’re not creating something that’s an investment product—that is a security.”).

Commissioner Peirce argument, the SEC would likely allege that purchasing tokens representing fractionalized ownership of an NFT likely constitutes an investment, and, in certain cases, that such fractionalized ownership qualifies as a common enterprise.<sup>184</sup> Nevertheless, it may be difficult to prove that a purchaser of fractionalized NFTs has a reasonable expectation of profits based on the efforts of others.<sup>185</sup> Especially if an NFT is merely fractionalized interests and sold without marketing statements indicating an increase in value, the SEC may not be able to prove any reasonable expectation of profits within the meaning of *Howey*.<sup>186</sup>

If NFT fractionalization and staking trigger securities regulations, creators and owners may be exposed to financial penalties and reputational damage under the Securities Act of 1933 and the Securities Exchange Act of 1934.<sup>187</sup> Moreover, once classified a security, the federal securities anti-touting provision requires individuals who promote crypto asset securities to disclose the nature, source, and amount of compensation they received in exchange for the promotion.<sup>188</sup> For example, Kim Kardashian was paid \$250,000 to publish a post on her Instagram account about EthereumMax (EMAX) tokens, a crypto asset security offered and sold by EMAX, without disclosing the payment she received for the promotion.<sup>189</sup> The SEC filed charges and Kardashian agreed to settle for touting, “pay[ing] \$1.26 million in penalties, disgorgement, and interest, and cooperating with the Commission’s ongoing investigation.”<sup>190</sup>

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184. See Pao et al., *supra* note 177.

185. *Id.*

186. *Id.*

187. 15 U.S.C. § 78a.

188. *ICO “Listing” Website Charged with Unlawfully Touting Digital Asset Securities*, U.S. SEC. & EXCH. COMM’N (July 14, 2021), <https://www.sec.gov/news/press-release/2021-125> [<https://perma.cc/Q4K3-975Y>].

189. Mike Calia, *Kim Kardashian pays over \$1 million to settle SEC charges linked to a crypto promo on her Instagram*, CNBC (Oct. 3, 2022), <https://www.cnbc.com/2022/10/03/kim-kardashian-settles-sec-charges-instagram-crypto-promotion.html> [<https://perma.cc/C2CV-5VDU>].

190. *SEC Charges Kim Kardashian for Unlawfully Touting Crypto Security*, U.S. SEC. & EXCH. COMM’N (Oct. 3, 2022), <https://www.sec.gov/news/press-release/2022-183> [<https://perma.cc/MTY5-X87D>].

VI. MINTED CONDITIONS: ANALYZING THE IMPORTANCE  
OF NFT LICENSING AGREEMENTS

Having defined and provided a historical account for NFTs, it is important to understand the relationship between the ownership of NFTs and the assets that may be associated with the NFT. An NFT is simply coding on a blockchain and does not describe the digital asset itself. NFTs are separate and distinct entities from the embedded IP content.<sup>191</sup> Above all, NFTs, unlike smart contracts, are executed and governed by fundamental contract law. Consequently, an NFT licensing agreement is a legal transfer of property rights between an NFT owner-licensor and an NFT licensee in exchange for some form of deal consideration, usually compensation.<sup>192</sup> The NFT license is designed to balance two concerns: protecting the creative labor and ingenuity of IP creators and granting users the freedom and flexibility to fully enjoy their digital assets.<sup>193</sup>

As a matter of legal due diligence, it is recommended that sellers wishing to transfer or assign IP rights draft strong, clear, and comprehensive NFT licensing agreements, and buyers read, understand, and assent to what they are purchasing. Additionally, NFT licenses should include terms on how subsequent purchasers may obtain ownership of such NFTs and associated rights. There is a spectrum of approaches to drafting an NFT licensing agreement.

*A. Ensuring the Scope of the Agreement Incorporates the Rights to the NFT*

At a minimum, a valid NFT licensing agreement must include three essential terms: the adequately described product, the price or monetary consideration, and the named parties.<sup>194</sup>

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191. For an analysis on the taxonomy and attributes of NFTs, see Fairfield, *supra* note 33.

192. Kyle Padden, *NFTs: What Are They and What Are Your Rights and Liabilities as an Owner*, Nw. J. TECH. & INTELL. PROP. (March 5, 2022), <https://jtip.law.northwestern.edu/2022/03/05/nfts-what-are-they-and-what-are-your-rights-and-liabilities-as-an-owner/> [<https://perma.cc/CGS7-H4T9>].

193. NFT LICENSE, <https://www.nftlicense.org> [<https://perma.cc/VL9L-YJ4K>] (last visited on Mar. 15, 2023).

194. At the very least, the “writing” must state with reasonable certainty: (a) the identity of both contracting parties; (b) the subject matter of the contract so that it can be identified either from the writing or if the writing is not clear by the aid of extrinsic evidence; (c) the essential terms and conditions of all the promises constituting the contract

The licensing agreement must clearly identify the “subject matter” of the digital asset being licensed or purchased, even if partially in code. This is important because a seller-licensor may possess the rights to, and need to account for, an inventory of various works and must ensure that only particular products are delivered to avoid future ownership complications. Another key component of the licensing agreement is a duration clause. This establishes the period for which the buyer-licensee has proper authority to perform any exclusive rights, such as minting and selling NFTs, and the rights are restored to the seller-licensor after the term has expired.

Typically, licensing agreements include specific provisions explaining any fees, future sale royalty structures, profit sharing, options, or other considerations associated with the sales of the work. Seller-licensors generally generate revenue in exchange for granting the buyer-licensee rights to the work, as well as certain percentages of the first and subsequent resales. Further, a licensing agreement must state the transfer of ownership to establish the rights being granted by the seller-licensor to the buyer-licensee for each work.<sup>195</sup>

The relationship of the parties plays a significant role as well. Customarily, a diligent NFT minter simply commissions artwork from a contracted artist on a work-for-hire basis.<sup>196</sup> This ensures that the minter, also called the commissioning party, is the owner of the copyrightable work that the contracting artist produced. Further, an employer-employee relationship, where a seller-licensor hires illustrators or graphic artists to mint NFTs as their primary job function, guarantees the employer-minter copyright ownership.<sup>197</sup>

Alternatively, independent artists and owners may retain copyright ownership by producing, or partnering with a third party to produce, NFTs based on their owned works to display, market, sell, or otherwise leverage and monetize in the NFT marketplace. In this way, it is analogous to the Coca-Cola Company selling its products to bottling and canning operators, distributors, and fountain retailers as a marketing

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and by whom and to whom the promises are made. RESTATEMENT SECOND OF CONTRACTS § 131 (Am. L. Inst. 1981).

195. 17 U.S.C. § 106.

196. Under general copyright principles, a copyright becomes the property of the author who created the work. However, work-for-hire is an exception to this principle and can be established through contract before a particular work is created. 17 U.S.C. § 101.

197. *Id.* The Copyright Act provides that a work prepared by an employee “within the scope of his or her employment” automatically vests with the employer as a “work made for hire.” *Id.*

strategy while never granting any underlying rights to its wealth of IP tied to the formula itself.

*B. Ensuring that the Parties Understand Their Obligations*

To avoid future litigation, sophisticated NFT sellers-licensors should draft licensing agreements distinguishing whether a buyer-licensee is granted ownership rights or merely permission to use. IP rights or ownership in the digital asset underlying the NFT transfers to the purchaser only if the owner of that asset expressly transfers those rights in a license agreement. If NFT minters or developers fail to obtain a signed licensing agreement before creating an NFT, there may be ownership problems pertaining to the underlying assets. These issues are compounded if the purchase agreement makes no mention of NFT rights conveyed.

Obligations may require that the artist produce high-quality artwork, deliver it promptly, and ensure that the rights, including copyrights, of any third party, are not infringed in its production. To optimize brand protection, it is important to include a quality control provision. Further, confidentiality statements create obligations binding the parties and preventing them from divulging sensitive information—like trade secrets and know-how—and indicating possible recourse in the event of a breach.<sup>198</sup>

Melanie Howard, Partner and Co-Chair of the Advanced Media & Technology Department at Loeb & Loeb LLP, identifies three main categories as illustrative and informative to license rights in underlying IP associated with the NFTs: (1) a “traditional” approach, where an NFT grants the owner access to, but no rights in, the underlying IP, similar to purchasing a physical painting; (2) a middle-ground approach, where some rights are granted in underlying IP; and (3) a “crypto-native” approach, where purchasing an NFT also grants full rights in the underlying IP.<sup>199</sup>

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198. See HOT WHEELS PURCHASE AND LICENSING AGREEMENT, [https://assets.contentstack.io/v3/assets/blt485dfa12bf05dba5/bltf6f3b16a2a6875a8/61bbc1ebdbddb351314036e7/Hot-Wheels\\_NFT\\_Purchase-and-License-Agreement.pdf](https://assets.contentstack.io/v3/assets/blt485dfa12bf05dba5/bltf6f3b16a2a6875a8/61bbc1ebdbddb351314036e7/Hot-Wheels_NFT_Purchase-and-License-Agreement.pdf) [<https://perma.cc/K5C4-ZPYC>].

199. Melanie J. Howard, *Brands and NFTs: Licensing and Contracting Considerations*, LOEB & LOEB LLP (April 2022), <https://www.loeb.com/en/insights/publications/2022/04/brands-and-nfts-licensing-and-contracting-considerations> [<https://perma.cc/43PM-N9KV>].



### 1. The “Traditional” Approach

Much like purchasing ordinary physical products, the traditional approach grants NFT purchasers limited rights to use the asset for personal use—namely, displaying it as a social media avatar or in a crypto wallet, or selling the NFT on the secondary market.<sup>200</sup>

For example, many people are familiar with the NBA Top Shot platform,<sup>201</sup> which was designed by the NFT Company Dapper Labs.<sup>202</sup> In the NBA Top Shot “Marketplace,” users can buy, trade, sell, and showcase short highlight videos from actual NBA games, called “Moments.”<sup>203</sup> NBA Top Shots purports to allow purchasers to “own” NBA moments, by granting an extremely limited—“non-exclusive, non-transferable, royalty-free”—license to use and view these moments only within the NBA Top Shot platform.<sup>204</sup> Because it is a private marketplace, the NFTs only have any real value when used in the “walled garden”<sup>205</sup> of the NBA Top Shots platform. If someone does not use the platform or website, the NFT does not have any functionality at all. Further, as the copyright holder, the NBA can prevent any display that conflicts with the original restrictive license granted by the NBA.<sup>206</sup>

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200. *Id.*

201. Dapper Labs, Inc., *Dapper Labs Opens NBA Top Shot Beta to All Fans*, PR NEWSWIRE (Oct. 1, 2020), <https://www.prnewswire.com/news-releases/dapper-labs-opens-nba-top-shot-beta-to-all-fans-301144010.html> [<https://perma.cc/7FSM-PD8T>]; NBA TOP SHOT, <https://nbatopshot.com> [<https://perma.cc/H847-BDRZ>] (last visited Mar. 15, 2023).

202. DAPPER LABS, <https://www.dapperlabs.com> [<https://perma.cc/ERB3-VC9P>] (last visited Mar. 15, 2023). Dapper Labs is a Vancouver-based blockchain company specializing in making video games. It has developed games such as CryptoKitties, NBA Top Shot, and UFC Strike. The company’s platform is known as Flow. It is a blockchain that allows for users to access consumer applications, games, and digital assets.

203. See Tommy Beer, *How Did a LeBron James Video Highlight Sell For \$71,455? A Look At A Burgeoning Product Called NBA Top Shot*, FORBES (Jan. 23, 2021), <https://www.forbes.com/sites/tommybeer/2021/01/23/how-did-a-lebron-james-video-highlight-sell-for-71455-a-look-at-a-burgeoning-product-called-nba-top-shot/?sh=6249838d184b> [<https://perma.cc/44KK-UKX5>] (describing NBA Top Shot as a “blockchain-based platform that allows fans to buy, sell[,] and trade numbered versions of specific video highlights”).

204. Saul Ewing Arnstein & Lehr LLP, *NBA Top Shot Moments—What Are You Actually Buying?*, JD SUPRA (Mar. 11, 2021), <https://www.jdsupra.com/legalnews/nba-top-shot-moments-what-are-you-3632095/> [<https://perma.cc/WBR5-6E48>].

205. Julien Mailland, *For an Anti-discrimination Act for Cyberspace: Two-Sided Pricing, Walled Gardens, and the Depletion of the Marketplace of Ideas*, 44 HASTINGS COMM. & ENT. L.J. 41, 62 (defining “walled gardens” as a series of closed platform ecosystems, where users could only access the content offered by those “gated communities”).

206. *Terms of Service*, NBA TOP SHOT (Aug. 31, 2022), <https://nbatopshot.com/terms> [<https://perma.cc/M6UX-B3T8>] (noting that if a user violates any terms of the license,

Ultimately, NFT purchasers receive limited rights to use the asset for personal use. Under the traditional approach, because purchasers do not own any copyrights to the original NBA video, ownership of a particular clip does not grant standing to enforce the copyright and exclude others from displaying the video elsewhere.<sup>207</sup>

## 2. The Middle-Ground Approach

The middle-ground approach gives creators limited rights to the underlying IP of the NFTs they purchase, allowing brands to harness the potential of Web3 to support creators.<sup>208</sup>

As an illustration, in December 2021, Nike extended its digital footprint into the Metaverse by acquiring digital fashion and 3-D creation company RTFKT (pronounced “artifact”).<sup>209</sup> Nike uses its famous trademarks, such as its “Nike,” “Just Do It,” and “Jordan” word marks, its iconic swoosh logo, the Jordan silhouette logo, and a stylized combination of its name and the swoosh,<sup>210</sup> on downloadable virtual goods. This is because “[t]hey’re filing new applications for the company’s main trademarks, saying that they’re going to launch and start selling virtual clothing, headwear, [and] shoes, in online and virtual worlds.”<sup>211</sup> Recently, Nike and RTFKT collaborated in launching the first digitized sneakers, dubbed Nike “Cryptokicks.”<sup>212</sup>

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Dapper Labs “may, at [their] sole and absolute discretion, and without notice or liability to you . . . immediately suspend or terminate your user account and/or delete your Moments’ images and descriptions[.]”).

207. According to the Federal Copyright Act, only “[t]he legal or beneficial owner of an exclusive right under a copyright is entitled [ ] to institute an action for any infringement of that particular right committed while he or she is the owner of it.” 17 U.S.C. § 501(b).

208. See Howard, *supra* note 199.

209. Don-Alvin Adegeest, *Nike acquires virtual sneaker and fashion start-up RTFKT*, FASHIONUNITED (Dec. 14, 2021), <https://fashionunited.com/news/business/nike-acquires-virtual-sneaker-and-fashion-start-up-rtfkt/2021121344484> [<https://perma.cc/V455-DC9F>].

210. *Nike Trademarks*, GERBEN TRADEMARK LIBRARY, <https://www.gerbenlaw.com/trademarks/footwear/nike/> [<https://perma.cc/AD89-LJSB>] (last visited Mar. 15, 2023).

211. Jessica Golden, *Nike is quietly preparing for the metaverse*, CNBC (Nov. 2, 2021), <https://www.cnbc.com/2021/11/02/nike-is-quietly-preparing-for-the-metaverse-.html> [<https://perma.cc/Z3RA-DQ3T>].

212. *RTFKT x Nike Dunk Genesis CRYPTOKICKS*, OPENSEA, <https://opensea.io/collection/rtfkt-nike-cryptokicks> (last visited Mar. 15, 2023). The digital sneakers arrive in the form of the brand’s iconic Dunk silhouette. The Nike Dunk Genesis kicks are customizable with eight skins made by RTFKT. Each skin can be applied to your virtual shoe by changing the “vial” that updates the look of the sneaker.

Similar to NBA Top Shots' terms and conditions, the RTFKT terms state that RTFKT retains all ownership of the underlying asset and grants a limited display right to the purchaser.<sup>213</sup> However, Nike-owned RTFKT grants commercial rights to "CloneX" NFT holders, allowing owners to launch derivative projects, mint fan art, and make and sell avatar-based merchandise, generating up to \$1 million in revenue.<sup>214</sup> By using this commercial license option, RTFKT grants two critical rights which distinguish it from NBA Top Shots' traditional approach: a limited right to commercialize the underlying asset, and the right to create derivative works.

### 3. The Crypto-Native Approach

Distinguishing themselves from many of the NFT collections released by established brands, Bored Ape Yacht Club has taken an innovative approach to transferring IP rights: when someone purchases a Bored Ape NFT, they own the NFT as well as the underlying asset and IP. According to the terms and 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.<sup>215</sup>

Because buying a Bored Ape NFT gives the buyer full IP ownership rights, owners have jumped at the chance to turn their Bored Apes into all kinds of media projects, including movies (The Degen Trilogy)<sup>216</sup>,

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213. See Howard, *supra* note 199.

214. Anushree Dave, *Nike-owned RTFKT grants CloneX holders commercial rights to NFTs*, THE BLOCK (July 6, 2022), <https://www.theblock.co/post/156015/nike-owned-rtfkt-grants-clonex-holders-commercial-rights-to-nfts> [<https://perma.cc/U7ZU-DHFP>].

215. *Terms of Service*, BORED APE YACHT CLUB, <https://boredapeyachtclub.com/#/terms> [<https://perma.cc/R9UZ-QRJY>] (last visited Mar. 15, 2023).

216. Daniel Van Boom, *Bored Ape Yacht Club Is Getting Its Own Film Trilogy*, CNET (Apr. 11, 2022), <https://www.cnet.com/personal-finance/bored-ape-yacht-club-is-getting-its-own-film-trilogy/> [<https://perma.cc/6ZW5-SKM9>].

music (Dancing Astronaut)<sup>217</sup>, podcasts (Two Bored Apes)<sup>218</sup>, books (All Gone, The Finest of Street Culture),<sup>219</sup> and apparel (Bored Ape Wear).<sup>220</sup> Some owners have even signed their Bored Apes to traditional talent agencies and music labels as an additional IP asset. Projects leveraging the IP of NFT collectives, such as Bored Ape Yacht Club, illustrate how a 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,<sup>221</sup> like Google or Apple, do not.

### C. Miscellaneous Boilerplate Provisions

The NFT licensing agreement also needs to include a clause laying out the consequences each party will face should it fail to deliver on its obligations. It is also recommended that the licensing agreement specify which jurisdiction will govern should any disagreement arise, preferably in a “plaintiff-friendly” forum favorable to NFT licensing. Because NFT-specific insurance policies for NFT creators, NFT owners, digital marketplaces, storage wallet providers,<sup>222</sup> and server farms<sup>223</sup> will develop over time, it is further recommended that the agreement bespeak coverage or no coverage for the near future. Also, if the buyer is given

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217. Cameron Defaria, *Universal Music announces Bored Ape Yacht Club music group*, DANCING ASTRONAUT (Nov. 17, 2021), <https://dancingastronaut.com/2021/11/universal-music-announces-new-bored-ape-yacht-club-music-group/> [<https://perma.cc/FJQ8-L5BG>].

218. TWO BORED APES PODCAST, <https://www.twoboredapes.com> [<https://perma.cc/62NA-R3GD>] (last visited Mar. 15, 2023).

219. LA MJC, ALL GONE-THE FINEST OF STREET CULTURE (2021).

220. BORED APE WEAR, <https://www.boredapewear.com> [<https://perma.cc/MQE8-DZYN>] (last visited Mar. 15, 2023).

221. Brad Gillum, *Branded House vs. House of Brands*, WILLOW MARKETING (July 18, 2018), [https://willowmarketing.com/2018/07/17/branded\\_house\\_vs\\_house\\_of\\_brands/](https://willowmarketing.com/2018/07/17/branded_house_vs_house_of_brands/) [<https://perma.cc/VN6W-FCCA>]. A Branded House is the most common form of brand architecture. Major brands like Google and Apple are exemplary models of this style, wherein both have smaller sub-brands, but all are marketed and operated under the umbrella of the parent brand. *Id.*

222. A wallet provider is an entity that provides a virtual currency wallet—namely, a means (software application or other mechanism/medium), for holding, storing, and transferring bitcoins or other virtual currency). A wallet holds the user’s private keys, which allow the user to spend virtual currency allocated to the virtual currency address in the block chain. *What is a crypto wallet?*, COINBASE, <https://www.coinbase.com/learn/crypto-basics/what-is-a-crypto-wallet> [<https://perma.cc/Z9S6-8Y7R>] (last visited Mar. 15, 2023).

223. A server farm is a group of computers acting as servers and housed together in a single location. *What is a server farm?*, GIGABYTE, <https://www.gigabyte.com/Glossary/server-farm> [<https://perma.cc/SYS3-4MRP>] (last visited Mar. 15, 2023).

cancellation rights or warranties, then the contract should precisely specify the remedy or remedies available to the parties. Finally, during the parties' due diligence process, warranties of title, authenticity, and continuing existence of the digital image as well as non-infringement and other standard warranties in the sale of goods should be procured.

#### VII. THE FUTURE OF NFTS IN THE WORLD OF WEB 3.0

Beginning as a means of tokenizing art and multimedia, NFTs have been involved in various use-cases in industries like finance, real estate, healthcare, insurance, and supply chains. Most NFT creators believe that deregulated and decentralized solutions best protect NFT collectors and the value underlying their digital assets.<sup>224</sup> This is because despite being highly accessible and sustainable, centralized NFT marketplaces (Web2 URLs) often store the NFT's actual images being tokenized separately from the code on the blockchain (a Web3 ecosystem) which provides the context for the representative asset.<sup>225</sup> Not only does this impede the prospect of using independent blockchain-based networks to build scalable frameworks with on-chain storage capabilities,<sup>226</sup> but it also affects the full enjoyment of their property interest in their digital assets.<sup>227</sup>

Putting the merits of the decentralization issue aside, NFT marketplaces would greatly benefit from more regulations. While NFTs undoubtedly hold aesthetic and intrinsic value, their inherent value is primarily derived from ownership interest in digitally scarce assets. This valuation depends too heavily on celebrity endorsements and propaganda from NFT enthusiasts, which makes NFTs vulnerable to market volatility and, eventually, market collapse.<sup>228</sup> As previously addressed, to the extent that NFT creators use staking and fractionalization to help raise money, the SEC may treat it as a security.<sup>229</sup> Further, to the extent

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224. Deepanshu Tripathi, *Centralization is Crippling—The Industry Needs Decentralized NFT Marketplaces*, NASDAQ (June 1, 2022) <https://www.nasdaq.com/articles/centralization-is-crippling-the-industry-needs-decentralized-nft-marketplaces> (“Promoting decentralized marketplaces is thus the viable and necessary alternative, a permanent solution.”).

225. *Id.*

226. *Id.*

227. See Fairfield, *supra* note 33.

228. Lara Williams, *The NFT market has collapsed (but that may not be a bad thing)*, INVESTMENT MONITOR (Aug. 21, 2022), <https://www.investmentmonitor.ai/crypto/nft-market-collapse-cryptocurrency-value> [<https://perma.cc/KR86-KG27>].

229. Ethan D. Trotz, *The Times They Are a Changin’: Surveying How the Howey Test Applies to Various Cryptocurrencies*, 11 ELON L. REV. 201, 205 (2019) (detailing how the

that the blockchain is being used to transfer value, it could be regulated as a money substitute by the Bank Secrecy Act.<sup>230</sup>

In the long run, the NFT asset class will greatly benefit from clearer regulations and guidance from the courts. One reason is that, without clear regulations, prudent investors avoid investing large capital in an unregulated space because the benefits of building a successful NFT enterprise and getting market exposure are outweighed by the prospect of having their cash reserve tied up in an unforeseeable legal battle.

Equally important, the NFT market crash and potential regulations could provide an opportunity for the NFT community to restore the creative use case of the tokens. The art industry has capitalized from the nonfungibility of NFTs—that is, their rarity and scarcity—and reduced NFTs to a tradable commodity. However, NFTs also denote ownership interests inherent in the token itself.<sup>231</sup> The token provides the utility and the value. The “value proposition”<sup>232</sup> of the NFT should lie in the utility of the token, whether that is providing access to exclusive live or virtual events, through NFT ticketing,<sup>233</sup> or buying and selling real-world

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“meteoric rise of cryptocurrencies presents significant uncertainties for both federal and state regulators” who must adjust to enforce the legal regulation of blockchains based on how people are using them).

230. Financial Crimes Enforcement Network, FIN-2019-G001, *Application of FinCEN’s Regulations to Certain Business Models Involving Convertible Virtual Currencies*, U.S. TREASURY (2019) (explaining how the Bank Secrecy Act does and may apply to “convertible virtual currencies”); see also *Requirements for Certain Transactions Involving Convertible Virtual Currency or Digital Assets*, 85 Fed. Reg. 83840, 83840–41 (Dec. 23, 2020) (to be codified at 31 C.F.R. 1010, 1020, and 1022) (“FinCEN is issuing this notice of proposed rulemaking to seek public comments on a proposal to require banks and money service businesses (‘MSBs’) to submit reports, keep records, and verify the identity of customers in relation to transactions involving convertible virtual currency (‘CVC’) or digital assets with legal tender status (‘legal tender digital assets’ or ‘LTDA’) held in un-hosted wallets (as defined below), or held in wallets hosted in a jurisdiction identified by FinCEN. FinCEN is proposing to adopt these requirements pursuant to the Bank Secrecy Act (‘BSA’). To effectuate certain of these proposed requirements, FinCEN proposes to prescribe by regulation that CVC and LTDA are ‘monetary instruments’ for purposes of the BSA.”).

231. See Ginsburg, *supra* note 1.

232. In marketing, a company’s value proposition is the full mix of benefits or economic value which it promises to deliver to the current and future customers (namely, a market segment) who will buy their products and/or services. Shane Mullin, *Value Proposition: Definition with 8 Winning Examples (2023)*, SHOPIFY (Dec. 1, 2022), <https://www.shopify.com/blog/value-proposition> [<https://perma.cc/X6WD-Z3MR>].

233. Langston Thomas, *NFT Tickets Are the Future of Live Music. Here’s Why*, NFT NOW (Oct. 26, 2022), <https://nftnow.com/features/nft-tickets-are-the-future-of-live-music/> [<https://perma.cc/YX4S-96B4>].

properties by recording the legal documents of the real estate transactions on the blockchain.<sup>234</sup>

More to the point, both entrepreneurs and sophisticated attorneys at the cutting edge of drafting contracts or IP rights would benefit from federal and state regulations and court doctrine. Meanwhile, transactional attorneys drafting NFT licensing agreements should ensure that the terms and conditions are embedded into the smart contract. As a point of reference, consider the case *Rensel v. Centra Tech, Inc.*,<sup>235</sup> filed in the United States District Court for the Southern District of Florida. In *Rensel*, the court determined whether a buyer, who purchased cryptocurrency by paying ether into a smart contract, was bound by the terms of an arbitration agreement that appeared on the seller's website and not in the smart contract.<sup>236</sup> United States Magistrate Judge Andrea M. Simonton noted that "a purchaser buying via the Smart Contract would not have had to agree to the terms of the Token Sale Agreement to complete the transaction nor offer direct evidence that the Plaintiff did agree to the terms of the Token Sale Agreement."<sup>237</sup> Because the buyer purchased the cryptocurrency directly through the smart contract, and not the website, he was not bound by the website's arbitration provision.<sup>238</sup>

#### VIII. CONCLUSION

Certainly, effective transactional drafting will ensure that terms and conditions are embedded in the "smart legal contract."<sup>239</sup> However, rather than being viewed as the technology to replace attorneys, the legal community should embrace smart legal contracts as an effective medium of transferring value, IP rights, and contractual agreements. Blockchain technology allows transactional attorneys and entrepreneurs to program

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234. Mike Butcher, *Propy launches NFT platform in the US, allowing real-world property to be bought as an NFT*, TECH CRUNCH (Jan. 27, 2022), <https://techcrunch.com/2022/01/27/propy-launches-nft-platform-in-the-us-allowing-real-world-property-to-be-bought-as-an-nft/> [<https://perma.cc/AS5S-NJ3Y>].

235. No. 17-24500-CIV-KING/SIMONTON 2018 U.S. Dist. LEXIS 100720 (S.D. Fla. June 14, 2018).

236. *Id.* at \*26.

237. *Id.* at \*27.

238. *Id.* at \*41.

239. Werbach & Cornell, *supra* note 43, at 322 ("The evolution from electronic, to data-oriented, to computable contracts embodies a trend toward greater machine autonomy. As computers can increasingly replace humans in negotiating, forming, performing, and enforcing contracts, contracts can increasingly operate with the speed and consistency of machines.").

different smart legal contracts to interact in innovative ways. For example, at closing, one smart legal contract can be programmed to buy a digital asset or a physical asset linked to an NFT at a set price, while another smart legal contract can be programmed to effectuate the transaction by selling the digital, or physical, asset.

Drafting NFT licensing agreements in the current legislative, regulatory, and judicial vacuum leaves much to be desired. Still, smart legal contracts offer quick, efficient, and effective ways to gather, organize, and record transactions, NFTs or otherwise. Once on the blockchain, legal transactions and public records will be easier to search and more readily available than current technology. Therefore, the legal industry can use the evolution of digital storage and recordkeeping to be more efficient, transparent, and cost effective—and ultimately, it can be used as an improvement and strengthening factor focused on pursuing clients' best interests.