Business Better (Season 2, Episode 19): NFTs and Your Business – Separating Fact From Fiction

Speakers: Brian Auerbach and Lara Ruggerio

Steve Burkhart:

Welcome to Business Better, a podcast designed to help businesses navigate the new normal. I'm your host, Steve Burkhart. After a long career at global consumer products company BIC – where I served as Vice President of Administration, General Counsel, and Secretary – I'm now Of Counsel in the Litigation Department at Ballard Spahr, a law firm with clients across industries and throughout the country.

Steve Burkhart:

In today's episode our lawyers discuss non-fungible tokens, better known as NFTs – including defining what an NFT is and is not, how to create one and post it to a marketplace, and the rights and responsibilities of ownership. Participating in this discussion are Brian Auerbach and Lara Ruggerio., both of whom Associates in Ballard's Philadelphia office. So now let's turn the episode over to Brian.

Brian Auerbach:

Good morning, loyal listeners. This is the Business Better podcast. My name's Brian Auerbach. I'm an intellectual property attorney here in our Philadelphia office.

Lara Ruggerio:

My name's Lara Ruggerio. I'm an associate attorney in the Philadelphia office as well, and I focus my practice on copyright and trademark prosecution.

Brian Auerbach:

I also do a little trademark and copyright prosecution as well, but I'm also an IP litigator. So we're a full service firm here. And today, we really wanted to talk about NFTs because NFTs are a hot button topic. There are a lot of interesting things happening in the legal and the business market. And since this is about how to make your business better, we wanted to talk about things like what is an NFT? What is not an NFT? What's going on in the wild world of NFTs? And if your business is considering making NFTs, how do you even make one. Lara, do you own any NFTs?

Lara Ruggerio:

No, I absolutely do not. I own cryptocurrency, as of today's date. Questionable idea, but yeah, not NFTs specifically.

Brian Auerbach:

Yeah, much like the crypto market, NFTs are an up and down market these days. It is a new technology, and there's a lot going on. And so part of what we're going to be talking about is things that a business should think about is if they're thinking about getting into the space. But before we talk about NFTs, I think we've got to talk about what NFTs are in the first place. And so let's start with the acronym.

Brian Auerbach:

So NFT, for those who are just coming onto the scene, or for those who listen to this podcast who haven't been inundated with other NFT materials, an NFT is what is called a non fungible token. So what does that even mean? So starting with token, a token is a token. A token represents something. I don't know. Lara, did you ever go to the arcade when you were a kid? Did you get arcade tokens, or did your arcade use quarters?

Lara Ruggerio:

Yeah, of course. Honestly I feel like I've interacted with both of those things.

Brian Auerbach:

Yeah, my childhood arcade definitely had tokens. And so a token is exactly what it sounds like. It is something that is supposed to represent something else. The more important term in here is non fungible.

Brian Auerbach:

And so what is fungibility? So fungibility is pretty much equatable to interchangeability. Can something be interchangeable? If it can, it's fungible. If it can't, it's non fungible. So a classic example when we're talking about money is our dollar bill system, our paper money. So I can have $100 bill. I can go to a bank, and I can say, "Bank, please change my $100 bill into five $20 bills or 20 $5 bills or 100 $1 bills." And each of those different types of currency split ups are equated to the $100 that I started with. So it's fungible. You can replace the five 20s with a $100 bill and vice versa. Likewise, metals can be fungible. Anything that basically sits in place of value is generally considered fungible.

Brian Auerbach:

When applied to the NFT scheme, NFTs, as we talked about earlier, are part of the broader crypto universe. And so for those who own cryptocurrencies, cryptocurrencies are fungible tokens. They are cryptographic tokens, but they are fungible. One Bitcoin represents the same value as any other Bitcoin. And it doesn't matter if you have Bitcoin A or Bitcoin B, they are fungible because they are interchangeable.

Brian Auerbach:

And that's the key. An NFT is a non fungible token. It is something that is unique, or for those lawyers who are listening, sui generis. It is something that is irreplaceable. And so gold itself might be fungible. A gold statue that is carefully crafted by an artist and that is only one of a kind, is non fungible.

Brian Auerbach:

Interestingly enough, when I was a very young attorney, I once had a client call me a fungible grunt monkey as I was working on his deal, because... I think he meant it as a joke, but pretty sure he just meant that I was replaceable.

Brian Auerbach:

So I think the lesson that I'm taking from most of this is I think we should all strive to be non fungible in our lives, in our practices. I think that's a good way to approach life.

Brian Auerbach:

But that's the key. So this is a non fungible token. It is something that is unique. So the question is, well, what's it a token to, and what does this all relate to? And so what we talked about earlier is the fact that NFTs exist in this broader universe of cryptocurrency. And the technology of NFTs is fascinating. And frankly, most of what Lara and I are talking about today could be the subject of its own entire podcast with multiple episodes. Because you can imagine, there's a lot of technology that goes into this. There's a lot of math, there's a lot of interesting cryptographic theories.

Brian Auerbach:

And we could really geek out on all of that, but we're not going to, because this is supposed to be a high level overview. But for those, again, who are new to this space, NFTs work in what I'll call the crypto universe. And the basis of the crypto universe is called the blockchain. And basically, a blockchain is a digitized, distributed ledger. So what is a distributed ledger? Most of us, when we go to a bank, they keep a ledger. They say, the bank says, you have $100 in your account. I take out $50. The bank keeps its ledger, updates it, and says you still have $50 in your account. All great.

Brian Auerbach:

The problem is that what is what a bank does, which is called a centralized ledger, is whoever owns the ledger, writes the rules. And so there's always a potential that the bank might make an error, there might be some something that happens where the bank turns around and says, "Oh, sorry, our ledger now says that you have $45, not 50."

Brian Auerbach:

And it's very hard for an outsider to authenticate that. One of the genesis of the blockchain system in this technology was to take ledger out of the hands of centralized authority and make it distributed, so that you, I, and everybody else who's participating has the ability to monitor and check on transactions.

Brian Auerbach:

And so, the idea is that as a transaction or a block is added to the chain, everybody agrees to keep their own copy of the ledger. And so, it's a majority consensus. So if 99 out of 100 ledgers say Brian sold $1 of Bitcoin to Lara, then if Laura's ledger says that I sold her $100 of Bitcoin, the majority ledgers would override that and say, nope, our public records show that it was only $1 and therefore that's all you get. But it takes the authority of the ledgering out of the hands of a centralized authority, and it brings it to you and I as participants in this.

Brian Auerbach:

Now there's many different blockchains and there's many, many different entities at play, but that is the rationale behind the NFT. A non fungible token is a block for the blockchain. It is a way to authenticate who owns what in a transaction. It is a way to record what happens on the blockchain. So again, it is using this publicly distributed ledger, which is supposed to be more accurate and more authentic, to track transactions.

Brian Auerbach:

So we've established what the basic technology is. So the question then is, so we've got a non fungible token, but what is the token? What do I actually get? Is it a thing? Is it something I hold in my hand? Is it something I download in my computer? The answer is no to basically most of those things. When we are talking about general NFTs, what an NFT is, it is a link that is stored on the blockchain. The token part, the ownership of the token, which is stored in a crypto wallet... So if anybody has, for instance, a coin based wallet or an Ethereum wallet, or any of the blockchain wallets out there, you can record a link as a block on the blockchain. The link points to some digital asset. It can be a file. It can be a movie. And part of what we'll talk today are the many different ways that companies have tried to digitize their assets.

Brian Auerbach:

But the token itself acts as proof of ownership as to what the link points to. And so having active links, and we'll talk about this later, is extremely important. But essentially, an NFT is supposed to be a public record of ownership of some piece of digital property. At core, that's what the NFT is. It is a digital receipt that in a perfect world is unassailable. It will show that you, the owner of the NFT, owns the property for which the NFT ties to.

Brian Auerbach:

Now, that's what an NFT is. I think it's more important to talk about what an NFT isn't. So Lara, what is an NFT not?

Lara Ruggerio:

Brian, I think you are right. I think for as much as people want to understand what NFTs are, and you have even a better understanding than I do. I think that you are non fungible, by the way. You're non fungible to me.

Brian Auerbach:

Thank you. You are also non fungible to me. I think we're all non fungible. And like I said, it just was a mean thing to say.

Lara Ruggerio:

It's creative. I'll give him... that is a creative insult. But I think what we have to think about is what are NFTs not. Fundamentally, an NFT is not a copyright in the work itself. Copyright can arise to the metadata, including the properties in artwork, or the software token, which is the code on the blockchain platform that Brian was talking about. But it's not a copyright in the work itself.

Lara Ruggerio:

I think the easiest way to explain this is with an example. So in January of 2022, an anonymous NFT acquisition group, that calls itself Spice, DAO, DAO standing for Decentralized Anonymous Organization, won a copy of Jodorowsky's Dune at an auction at Christie's. The appraisal for this original copy of this renowned, famous, and beloved work was about $40,000. The auction started, it was going as they expected. Then all of a sudden, Spice DAO came in and bought the book for about 2.66 million euros, which of course blew the $40,000 appraisal out the water. Spice DAO, proudly tweeted, "Look what we bought. We bought this book. This is ours now. We own Dune. We're going to symbolically burn this book, and we're going to have a video of the burning book, and it's going to be an NFT. And then we're going to make a series of NFTs based on the book. And we're going to make an animated series inspired by the book."

Lara Ruggerio:

And there's of course, the official judicial system, then there's the court of Twitter that quickly, quickly confirmed with Spice DAO that owning this single old book does not confer copyright in the work itself. It just means you own that super cool single old book. So of course, Spice DAO has since said, "Oh no, no, no, we didn't think we owned it." I think they got stuck. And now they do have a copy of this really cool book, but they surely do not own the rights to Dune.

Brian Auerbach:

So, would you say that the spice did not flow?

Lara Ruggerio:

I think so. Maybe they went it a little too spicy. I don't know exactly what it is, but-

Brian Auerbach:

Sorry, Lara, that is Dune reference. And I apologize for springing you on a Dune reference. But yes, in this case, for those Dune aficionados out there, those who control the NFTs control the universe, and the spice company did not succeed. So in this case, the spice did not flow. So there is your obligatory Dune quote for the day. Lara, please continue.

Lara Ruggerio:

Honestly, I just know that it's beloved. Unfortunately, I'm not one of those people who love it, but I'm again, happy for you, happy you threw in the quote. But that's about it for me on what NFTs are not.

Brian Auerbach:

Yeah. NFTs, and this is important to remember, because again, this is an emerging technology. I think NFTs as a concept are 10 years old at most. The blockchain, as a whole, the whole concept of a blockchain and Bitcoin is still, we are within the first 30 years of this technology and everybody is figuring it out. And there's always a concern. And part of this podcast is not just for those listeners who are business owners or lawyers who are consulting with businesses, but also for people as people, and to always make sure that you understand what you're buying and what you are not buying. And in this case, a 2.6 million Euro buy for essentially a receipt of ownership of a book, but not the book.

Brian Auerbach:

And I'm sure we can have a whole podcast, there's an entire scheme of law having to do with copyright about how ownership of the thing is not the ownership of the copyright in the thing. And there are very famous cases, and this is exactly a similar situation where an ownership of the NFT doesn't necessarily mean that you have rights to exploit the original work. And so that is always something to be careful of, especially if somebody is selling you an NFT and claiming that they are also transferring the rights to something in that, which requires more than just the sale of an NFT. But that is a subject probably for its own podcast.

Brian Auerbach:

So we've talked about what is an NFT, we've talked about what an NFT is not. So the question is, how do you do it? What do you need to do to even an NFT? And the answer is not much, to get off the ground running. There are of course, with any new business, there are significant other businesses that have popped up. But here's the general overview. And again, we could dive into the weeds in this probably for several podcasts, because you can also do it yourself. And there's a lot of technical knowhow that goes into it.

Brian Auerbach:

So generally, the first thing that you have to do, if you want to create an NFT, is you got to decide, what do you want to create an NFT of? And so from a business consideration, there's a few things to keep in mind, which is, is this something that will be a good NFT? Part of the issue that has been coming up over and over and over, and we'll talk about some of these issues later, is that just because you have receipt of ownership doesn't necessarily mean that you have control of the underlying property. And so there is a lot of concern in the NFT world right now, where NFTs are being minted, so NFTs are being created, but people are copying the underlying image. And we live in a digital world. So if somebody, for instance, has an NFT of the Nyan Cat... I don't know if anybody, Lara, have you seen Nyan Cat?

Lara Ruggerio:

No, but that seems like something I would like.

Brian Auerbach:

Yawn cat is an early meme. It's a cat that has Pop-Tarts on its sides, and that is flying through space and has rainbows coming out the back.

Lara Ruggerio:

I'm familiar with the rainbow riding Pop-Tart cat. Yes. I didn't know that this cat had a name.

Brian Auerbach:

Yes. That is Nyan Cat, and that cat was famously turned into an NFT, one of the first big money NFTs that was sold. The problem is that there are images of Nyan Cat all over online, and it's very easy to, what some people derogatory say is the right clickers, where you can right click and save as the picture, and you've got your own copy of the asset. And part of also what is coming up is that people are taking their own copies of the digital work, making their own NFTs, and then there are two competing blockchain entries where one link is owned by one person, one link is owned by the other, but it's all the same underlying property. And so there's a lot of ownership issues that still have to get worked out.

Brian Auerbach:

The point of this is, is what you are selling something that is easily replicable, or is this something that you can maintain its uniqueness? And when we think about it in terms of an intellectual property context, for me, I think of it in terms of trade secret law. So good trade secrets are things that are not easily discoverable, are things that can't really be reverse engineered. Because the value of a trade secret is only for so long as you can keep it a secret. And here's the same thing, and NFTs, one of the bases of its value is its uniqueness.

Brian Auerbach:

And so when you're considering whether or not your business wants to have minting of NFTs be part of the businesses, how easy or difficult would it be to secure that asset on the backend? So if you are minting an NFT of something, can anyone go to your website and just download the original? Because if they can, maybe that's not the best thing to start minting NFTs. But there are many, many different other options out there in terms of what you can mint. And so it's something to keep in mind as you are going through.

Brian Auerbach:

So once you have picked your NFT, you also have to put it somewhere where there's a link. And this, like we said, an NFT is essentially a link that is engraved onto the blockchain. So one of the other major considerations that a company should have is how secure and how long lasting are my links. Meaning there's a theory, or there's a phenomenon that's been going on as the internet gets older, which is called link rot. And the idea is that links that maybe worked five years ago might not work anymore. And so, the problem is if you've got an NFT that designates a specific link, that's supposed to go to a specific digital asset, and that link breaks, either because you lose the domain name registration, or because you change the domain registration, or because the server breaks, then you might have an engraved link to nowhere.

Brian Auerbach:

And this is not so much a concern for NFT sellers, because chances are your links are secure, but certainly for those who are buying NFT assets, one of the questions that you should be asking is how secure is this link, and how durable is this property going to be? And so for those businesses that are considering making NFTs, another consideration should be is how robust is our domain presence? How robust can we make these links, so that the people who are receiving them will have the ability to enjoy the digital asset that they are buying in perpetuity. So another consideration to have.

Brian Auerbach:

So we've picked our NFT, we've got our link set up. The next part is we've got to get that NFT onto the blockchain. So you have to pick a blockchain. Now, I won't profess to know all of the blockchains. There are major ones like Ethereum, which is probably the biggest traded, one of the main NFT... I think it was the first blockchain to be able to accept NFTs on the chain. But there of course have been a million other blockchains that have popped up. And again, each one is its own set of distributed ledgers. So when I say a blockchain, essentially you can think of it as that distributed ledger. So Ethereum has a set of folks who have that distributed blockchain. There are others that have their own independent RI distributions.

Brian Auerbach:

And so there are considerations that the company could should make. One is the fees that are charged. Every blockchain charges its own separate type of fees. And generally, there are always transaction costs when you are making transactions on the blockchain. In the Ethereum world, they call it Ethereum gas. But that's something to consider is what are the fees going to be, especially if the business is going to be minting a lot of NFTs and trying to sell them. You don't want the fees to be prohibitive.

Brian Auerbach:

The other thing to think about is how secure is the distributed ledger. So for Ethereum or for some of those ledgers that have been in use for a long time, those are probably good because they have a significant amount of users. There's a significant amount of distribution. But if your blockchain only has two keepers, there's a potential issue that the amount of things that can authenticate that blockchain are now almost centralized. And so it's very important for a business to consider how secure do they want that ledger to be and how authentic it can be.

Brian Auerbach:

Now, you don't have to pick a blockchain. There are also, there is the ability to create your own smart contracts and basically sell your own NFTs. And this easily could also be its own 10 part episode. But I think a smart contract is a really interesting concept.

Brian Auerbach:

Smart contracts are basically the digitization of legal agreements. And so for those listeners who might have programming backgrounds, it's almost an if/then statement. So a classic smart contract is a vending machine. A vending machine contract is if I insert $1, then I will get a soda. I insert my dollar, I get my soda. Contract performed. But that's hard coded into the machine. It knows that when I insert the dollar and I press the right button, it has to deliver the soda. And so a smart contract is a self-performing contract that utilizes digital technology. And it underlies the basis for all of that. And companies can go in and create their own smart contracts that govern what happens on the back end of an NFT.

Brian Auerbach:

So one of the interesting things that is being explored in the NFT world is using them as an ability for royalty payments. The idea being that you could program a smart contract to say that if this particular NFT gets sold, 50% of the proceeds automatically go to person A, and 50% of the proceeds automatically go to person B in perpetuity. So there's been a lot of discussion, particularly when we're talking about NFTs that tie to digital music or digital media, where royalties can be paid automatically via smart contract. The same way that vending machine knows to give me a soda if I give it a dollar, this smart contract says, if this NFT gets sold, a certain amount of the proceeds, which sometimes are in the form of Bitcoin, get distributed to this wallet and certain get distributed to that wallet. And it's a way to hard code in royalties into an asset, which is a fascinating idea, but it's also, again, fraught with potential complications.

Brian Auerbach:

So the point of this again, is to say, is that you can start from a preexisting system like Ethereum, or you can leverage what has now started to be a significant amount of code into creating your own smart contracts and doing your own NFTs, but it's very resource intensive.

Brian Auerbach:

So then you've got your blockchain picked, you've got your NFT selected. The next thing you have to make sure that you have is some form of crypto wallet. So again, examples of big players in the space, Coinbase is the one that comes to mind to me, mostly just because I have a friend who works there, but there are plenty of wallets. The main thing to be concerned about is does your wallet talk to the particular blockchain that you are putting your NFT on? Now, most of the major wallets are probably going to speak to most of the major blockchains. And every crypto is on its own. There's a Bitcoin blockchain. There's an Ethereum blockchain. Every single one of the cryptocurrencies has their own blockchain, and so it depends on where you want to put it.

Brian Auerbach:

Once you get that, once you get your wallet, make sure that you keep your seed keys handy. So many wallets come with recovery keys, and make sure you keep them. Because one thing that we have learned after now decades of crypto investment is that once it's gone, it's gone. And if you lose your key, you might be losing a whole lot of assets. So always make sure that you keep your recovery keys handy because you definitely don't want to be the person that lost their digital wallet and lost a lot of... Some people, their stories have hundreds of millions of dollars of crypto going missing because people either lose their keys, or the keys fail.

Brian Auerbach:

But once you have your wallet, your blockchain and your NFT, then you can get rolling. And there are companies that will help you get started right off the ground, so that you don't pay any transaction fees until you sell the NFT. But they usually don't put it on the blockchain until they're sold. There's some that put it on the blockchain immediately, but you have to pay transaction fees. And so there's many different ways to get into the NFT space. The most important things to remember are, again, is this something you want to make into an NFT in the first place? And two, is this going to be something that is sustainable for the business in the long run?

Brian Auerbach:

But it is still the wild west. And so there's been a lot of action by big companies. And we wanted to let everybody know about some of the major updates. And I think Lara, maybe start where you want. There's so much to talk about.

Lara Ruggerio:

Brian, I'm just sitting here thinking about what were my passwords 10 years ago, and would I gamble $100 million on being able to guess my password from 10 years ago? The answer is no. I can't tell you what my Starbucks password is. I use it every single day.

Brian Auerbach:

Yeah. Well, you have to write those down. So I know... I have a Trezor, which is a physical device that you can keep crypto on, and that comes with what are called seed keys. So it's 12 words in a particular order. And I have those written down somewhere because that's what you use to recover your wallet. So you definitely... Yeah. You got to be careful because it's not just passwords, but it's also recovery keys. So if you ever "lose" your wallet, if you want to reconstitute it, can't lose those seed keys.

Lara Ruggerio:

So you're telling me now I don't have to remember one word with eight letters and numbers and symbols, I have to remember 12 separate words?

Brian Auerbach:

I don't think you have to remember them, but I would say probably write them down.

Lara Ruggerio:

Brian, I think you're more in the weeds with this than I am. And in terms of thinking about the wild west and what is happening in the world of making NFTs and distributing NFTs and particularly how it relates to intellectual property, I want to talk about three different things. The first is trademark lawsuits. The second is copyright lawsuits. And the third is just a general overview of how NFTs might play out internationally. So let's start with trademark lawsuits.

Lara Ruggerio:

The first thing to keep in mind is that expressive works are not often found to violate trademark rights. Think Andy Warhol, Campbell soup cans in the early 1960s. As an artist, he decided this is what he was going to do. It's one of the, I would say one of the most iconic images in American history. No affiliation with Campbell's, just did his thing. Great free advertising for

Campbell's, but still I'm fairly certain that wasn't the result of a licensing deal or anything like that. So the underlying work, which would be that image, is held to be artistic expression.

Lara Ruggerio:

And in terms of using trademark in the title, artists are given a lot of leeway. Using trademark in a title is generally trademark infringement only if the title has no relevance to the work or explicitly misleads customers. So most of trademark law is centered around protecting the consumer. So that's pretty consistent with that. If I call my work, this is an advertisement for Campbell soup, and it's in fact not an advertisement for Campbell soup, that's going to confuse people. So that's not okay, but otherwise, generally artists have a ton of leeway.

Lara Ruggerio:

But now we get into this area where people are making NFTs, and they're using famous trademarks, or they're making some changes to what we would consider famous images. The first lawsuit I want to talk about, it was actually just a recent ruling, which is exciting, Hermes sued the creator of an unbelievably valuable set of NFTs, MetaBirkins. So Hermes makes these Birkin bags. I would say they're one of the most incredible symbols of wealth and the pinnacle of fashion in our society. I don't have one. Brian, I'm going to venture a guess that you do not carry a Birkin because I would've commented on it already.

Brian Auerbach:

I have heard of the Birkin bag, but, but I do not covet it. I know my wife does, but I don't think she has one either, to my knowledge.

Lara Ruggerio:

You would know.

Brian Auerbach:

I probably would know.

Lara Ruggerio:

You would know. Yeah. I think it would probably have its own insurance policy in your home. So then I'm going to say, Brian, as someone I'm going to say you're not the most familiar with fashion brand. So the fact that you know of Birkins, like I know of Dune as a concept, that means it's pretty substantial in society.

Lara Ruggerio:

So MetaBirkin arrives on the scene, describes itself as a digital art project by this artist, Mason Rothschild, and it's on the Ethereum blockchain. So these MetaBirkin NFTs are images of what appear to be fuzzy or furry versions of Birkin bags. And Birkin bags have a pretty distinctive shape and handles and proportions, and it appears to be fuzzy versions of those. Earlier today I looked up, there is a, for example, it looks like zebra fur in the shape of a Birkin bag. There's 100 of them. And these have sold for up to tens of thousands of dollars, which is on par for the bags themselves, the physical bags that you would purchase. For example, this furry zebra bag is currently available for just over $6,000.

Lara Ruggerio:

So they own the domain, metabirkin.com. They own social media handles, or they utilize social media handles MetaBirkin. And the funniest thing I saw looking at their materials today was there's a disclaimer on the MetaBirkins website saying they are not affiliated with Hermes, they're their own entity, everything like that, even though very clearly Birkin is a famous trademark belonging to Hermes. But the Birkin trademark recites leather bags as goods, handbags, purses, whatever you want to call them, not NFTs.

Lara Ruggerio:

So Hermes is suing this artist for trademark infringement, trademark dilution, and cyber squatting. So the most recent ruling, which I think was just a few weeks ago, the court found that the MetaBirkins were digital images that were this artistic expression, like Andy Warhol's Campbell's soup, and they were thus entitled to first amendment protection, which it's sad for Hermes. Great for the artist, sad for Hermes. But the artist had filed a motion to dismiss Hermes' lawsuit because the use of MetaBirkins as a title has no relevance to the work at all. It explicitly misleads customers. If I saw something that said MetaBirkins and wasn't familiar with this series of NFTs or didn't know that it wasn't affiliated, I would think it was affiliated. And that's exactly what the court wants to prevent from happening.

Lara Ruggerio:

So the court is now probably going to try and untie exactly what that means and see if there really would be a likelihood of confusion there, but it did not grant the artist's request to dismiss the matter in its entirety, because that's something that should be explored further.

Brian Auerbach:

So just to make sure I understand. So this is something where they're called MetaBirkins. And so the court said, hey, making these furry digital images of a Birkin, that's protectable under the first amendment. But we are not going to totally throw out the lawsuit that says it's not a problem for you to call them MetaBirkins.

Lara Ruggerio:

Yes. So my understanding is that Hermes sued for trademark infringement, dilution, and cyber squatting. Cyber squatting would refer to the use of the domain name, probably most specifically the domain name amongst other social media handles, et cetera. The trademark infringement and dilution would be using Birkin, because that's undoubtedly a famous trademark. So I think that's now where the court will focus its efforts, as opposed to looking more closely into the digital images. And if using the, I guess, distinctive shape and the handles of the Birkin bag itself would be a violation of Hermes' intellectual property rights. But again, I think things are changing so quickly. This may or may not be upheld by the next court that inevitably reviews these issues.

Brian Auerbach:

And I think the thing to take away, though, especially for business owners, is it's not just enough to do some diligence as to what you are making the NFT of. But also, you need to think about what you are titling the NFT, because that could potentially engender liability, even if the underlying image or asset that you're selling is yours original. So there's always nuance to all of this.

Lara Ruggerio:

Absolutely. Absolutely. The next one, I guess it's different, and I'm going to say it's less of a high fashion example, but given the prices that these shoes are worth, it's pretty high fashion. So Nike is suing StockX. And StockX, what they do is they purchase, I guess in bulk, limited edition releases of sneakers by Nike, they store them in these vaults, and then they sell NFTs. And according to StockX, its NFTs are basically claim tickets to access this pair of physical shoes and provide the owner proof of ownership and authenticity. So Nike of course is like, "No. No, no, no. You're using our trademarks and our logos." They just revised the complaint in May to add claims of counterfeiting and false advertising because Nike alleges that StockX is saying these are 100% verified, authentic Nike shoes, and StockX is looking to trade on the reputation and appeal of the Nike brand, which has extraordinary, undeniable cache.

Lara Ruggerio:

So there's some now discussion whether the digital tokens as products are distinct from the shoes themselves, or if the digital tokens, the NFTs, are inherently related to the physical product. So parsing that out will become its own separate issue. Nike claims that StockX is treating the NFTs as separate products, because when you go to their website, there's a whole category of NFTs, and you purchase the NFT and then you get an email that says something like, Congratulations, this is your new NFT." And StockX says, "No, these are just a digital receipt. It's a claim ticket for this pair of physical shoes."

Lara Ruggerio:

So especially because Nike just revised the complaint, I will be absolutely fascinated to see how this shakes out. Because StockX is using Nike's brand all over the place, all over the place, but that's also, I guess, the content of what they say they're selling, the claim tickets for the physical product.

Lara Ruggerio:

So those are two what I think are very interesting trademark examples, that whether you are more in two shoes or handbags, as opposed to Dune, whatever Dune is about, might appeal to you, or at least these are names you know.

Lara Ruggerio:

The next category, aside from trademark infringement, which is something the courts will have to shake out, is copyright. So I think the most compelling issue with copyright NFTs is oftentimes what we think of as valuable copyrighted works are co-owned. So for example, Jay-Z is suing his Rock-A-Fella Records co-founder, Damon Dash, because Dash wanted to create and distribute an NFT of Jay-Z's Reasonable Doubt album cover. According to the internet, there is some bad blood between Jay-Z and Damon Dash. That aside, this poses a fascinating intellectual property copyright question, because the copyright to the album is shared by Jay-Z, Rock-A-Fella Records, and Dash in one-third shares.

Lara Ruggerio:

So thinking about whether Dash would have the authority to issue an NFT based on this work, he only owns a third of it. So particularly in the music industry, when you think about how many people own portions of copyright to a piece of music, shaking that down and breaking it out will become very complicated very quickly. So this suit was just filed in June of 2021, but I think that watching how this shakes out will have huge implications for the music industry.

Lara Ruggerio:

The second matter deals with Pulp Fiction. So Quentin Tarantino, the director of Pulp Fiction, wanted to sell NFTs of seven different scenes from Pulp Fiction, with his commentary with the scene. And from what I understand, most of the time directors assign all of their copyright rights to the film studio, but in this case, Tarantino reserved some rights, but now Miramax is suing him because there's absolutely some debate there. And although this might seem more like a contract issue than a copyright issue, it still will have implications for how courts and businesses want to handle issues of copyright in NFTs.

Lara Ruggerio:

The last thing I want to talk about is how this will be handled internationally. When we think about enforcement or lawsuits, one of our first questions is where is this happening? Where is this going on? And when you talk about NFTs and blockchain and all of the big words Brian used before, we have to think about it's everywhere and it's nowhere.

Lara Ruggerio:

So in terms of how international jurisdictions will rule on NFTs, well, it would be ideal if there was some consistency. At this point, there isn't enough to know whether it's going to be consistent or not.

Lara Ruggerio:

For example, let's talk about China. When we talk about intellectual property and international protection of intellectual property or enforcement, oftentimes as a US-based attorney, we turn to China.

Lara Ruggerio:

So recently, the [foreign language 00:41:06] internet court ruled on a copyright infringement case related to an NFT. And the court, I guess, ruled on some issues, and most importantly, they gave some sense of where they will land on NFTs. The first great takeaway that's consistent with the US is that sale of the NFT does not mean transfer or license of the IP of the underlying work. And the second big takeaway is the legitimate creator of an NFT should be the person who owns copyright to or has license to the underlying work. So while at this point... There was a whole bunch of other things in there, but in my mind, those are two really, really big issues that will continue to be big issues in NFTs, creation of NFTs, distribution of NFTs, and enforcement when it relates to NFTs.

Lara Ruggerio:

So the fact that, shockingly, China and the US seem to be at least trending in the right direction on these big two issues, I would like to think is a good thing. And particularly for businesses that oftentimes now, especially if you're in products and you're shipping internationally, I think that this is a great sign, but of course we'll have to see how this shakes out, and we'll have to see how other jurisdictions begin to handle NFTs as well.

Brian Auerbach:

See, that stuff to me is just so fascinating. To me, this law, I feel like we're in the Napster era again, where the courts are trying to figure out new technologies as applied to, frankly, decades old IP laws. Our copyright act is the copyright act of 1976. And even though it's had updates over the years, it was created before computers were so ubiquitous. The digital millennium copyright act was around the year 2000, and we're 22 years from that. And as always, the law usually lags behind technology. And so, this is going to be a very, very interesting area. And it's a cautionary tale to those who are considering making NFTs be a big part of their business, because it is really the wild, wild west.

Brian Auerbach:

And generally, the courts tend to come out equitable. I will imagine there will be a set of common law that gets developed, much like there is common law surrounding rights of publicity, which is not really codified in any IP scheme. It doesn't really fit into copyright. It doesn't really fit into trademark. It doesn't really fit into patents, but there are rights that famous people, and frankly, every one of us has to our own likeness. And there has over the years been this massive body of common law that deals with how you should treat people's likenesses and what that is worth from an intellectual property, and frankly, just a general legal property standpoint.

Brian Auerbach:

And I feel like NFTs are probably going to go the same way. I would not be surprised if common law starts to shake out that at least as to blatant copies. If somebody makes an NFT out of an NFT, it might be very easy for a court to say, well, that's inequitable. But some of these are really fascinating.

Brian Auerbach:

I really like the Jay-Z one because I think that goes back to the idea that had been floated around a while ago, which is using NFTs as an example of smart contracts to code in royalty structures. It's a fascinating idea of music in the blockchain industry and using these smart contracts in a way that avoids disputes. And for those who are legal practitioners who are listening to this, this could be a way to modernize and streamline certain contracts that normally in the real world required an immense amount of diligence, especially when you're talking about 5, 10, 15, 20 years later, and trying to figure out who really has the rights, or even if you can figure out who has the rights, at least who's supposed to get a cut of the royalties decades after you've recorded an album.

Brian Auerbach:

It's really interesting. The wild west of legal, especially when it meets technology, always comes up with very, very interesting scenarios. But like we were saying, the thing to keep in mind is a court might have a very different interpretation of what an NFT is, versus what Twitter or the blockchain universe thinks. And sometimes courts get it. Sometimes they don't. And in many cases, it will take a lot of successive cases before there's really a clear consensus as to what an NFT really covers, what rights it gives, how you separate the NFT from the asset itself. There are just a lot of issues inherent. And so we just urge caution because no one knows what the next court case may bring.

Brian Auerbach:

And unfortunately, the nature of our court system is that it takes something going wrong. So NFTs have been around for a couple of years now in terms of mainstream use. And it's only just now that these cases are really getting to a point where decisions are being made and some guidance can actually be helpful. And so we are reaching a point of NFTs where crypto was a few years ago, where there were questions as to, well, how should it be taxed? How should it be regulated? Who has authority on this? What does the SEC have to do with all this? And over the years, there has been more distillation, but that is still also very, very new. And our government and our legal system is still trying to get its head around how do we treat these things with laws that were written before some of this technology was even envisioned, and how do we apply it to an older set of laws?

Brian Auerbach:

And so, yeah, I agree with you. I think this is going to be fascinating to watch how this plays out in the courts. So I think the thing that we really want to reiterate on this podcast is the one thing that China and the US really seem to agree on so far in the courts is that NFT ownership is not the same thing as ownership as of the IP. And I think the common theme that we are seeing through all of these cases in most of these disputes is people buying things or selling things, thinking that they have the right to buy or sell them, when there are other schemas at work, there are other laws at work, there are other things at work.

Brian Auerbach:

And so the lesson, if there's a takeaway from this episode of the podcast, is just be careful. Be careful when you're selling them, be careful what you call them. And certainly if you buy them, be careful at what you do with them. Because as the Spice DAO folks found out a very costly lesson, just buying the thing does not necessarily mean you bought the copyright in the thing, or the right... And copyright is the right to reproduce, the right to display, the right to transmit. And if you don't own those rights, then like the Spice DAO folks found out, just because you bought an NFT of Dune, of a particular version of a book of Dune, does not mean that you have the rights to Dune as a whole. And so be careful from a business standpoint, for acquisition of NFTs, and know what you are buying.

Brian Auerbach:

Lara, what about you? Do you have any tips in terms of NFTs?

Lara Ruggerio:

My other big takeaway here would be, and perhaps I'm biased because I tend to do a lot of brand based enforcement, trademark enforcement work, is that enforcement is going to be key here. Regardless of where the courts shake out on NFTs and ownership and any of these issues, if nothing else, if you are a brand and you find out that someone is using your brand name or photos of your product, or distributing something that you think is yours in an inappropriate way, you should take some type of action. Again, regardless of how the courts shake out, enforcement early and often is key to protecting your brand.

Lara Ruggerio:

Consider understanding the major players in the NFT space. OpenC, crypto.com, Binance, Wearable, Enjin, Nifty Gateway. There's enough that it's worth your time and effort to at least understand if and how someone might be misusing your brand or your product or whatever it might be. Enforcement early and often is key.

Brian Auerbach:

Well, that's that for this episode of Business Better. We hope this was helpful to everybody. As we hopefully have demonstrated in this time, there are a plethora of issues related to NFTs. And so if your business is considering buying them or selling them, we urge you to contact counsel, whether or not it's us here at Ballard, or whether it's your own, other attorneys. But again, as with any asset that a company is thinking of buying or selling, the key is diligence. Don't jump right into the deep end. Take a minute. Research what you're doing. Research the asset. Research whether or not this is something that you have the rights to. And if you do and you've got a path forward, then good luck and happy business.

Steve Burkhart:

Thanks again to Brian Auerbach and Lara Ruggerio. Make sure to visit our website, www.ballardspahr.com where you can find the latest news and guidance from our attorneys. Subscribe to the show in Apple Podcasts, Google Play, Spotify, or your favorite podcast platform. If you have any questions or suggestions for the show, please email podcast@ballardspahr.com. Stay tuned for a new episode coming soon. Thank you for listening.