ABA Forum on the Sports and Entertainment Industries – 2022 Annual Meeting

Four Seasons Hotel, Las Vegas, NV

Litigation Update – Oct. 7, 2022

NFT Litigation – Presented by David M. Given

A- Introduction

NFT stands for "nonfungible token." An NFT is a unique digital identifier written in computer code that when intended can point to a digital version of a creative work. An NFT cannot be copied, substituted, or subdivided, and is recorded in a blockchain (a distributed network of servers) to certify authenticity and ownership. The value proposition in NFTs flows from their non-fungibility.

Just as anyone can start a species of (fungible) cryptocurrency, anyone can create or "mint" an NFT. (The technical specifications for doing so are beyond the purview of this presentation.) While most of the nascent litigation over NFTs involves intellectual property issues, that litigation has also touched upon matters of securities law.

Ownership of an NFT does not ipso facto convey unlimited intellectual property rights to the underlying creative works they embody. Sometimes by agreement NFTs will convey rights like the copyright to a sound recording or video clip, thereby enhancing their value. Litigation in this area has tended to focus on the right of the issuer of the NFT to grant those rights as well as how an issuer may use others' intellectual property in minting and identifying the NFT.

B- Emerging NFT Cases

There are currently no appellate decisions in this area. So there is no "case law" per se, although there has been one notable federal district court decision.

In June of this year, U.S. Senators Patrick Leahy and Thom Tillis posed a series of questions to the U.S. Patent and Trademark Office and the U.S. Copyright Office aimed at determining whether the growth in the use of NFTs required changes in statutory law and the respective office's regulations. Both offices recently agreed to undertake a study to that effect, to be completed within the year.

1. Nike v. StockX

Facts:

StockX is an online resale platform (think: Ebay). It facilitates the marketplace for high end merchandise and collectibles, including sneakers.

Everyone knows Nike. And therein lies the rub.

Earlier this year StockX began minting NFTs associated with the product offered for sale on its site. It did so, it said, to allow users to verify the authenticity and ownership of that product.

But StockX went a step further. Via its "Vault NFT" program, it allowed users to trade possession of NFTs in lieu of possession of the underlying physical product. According to StockX, that scenario would facilitate the buying and selling of product by removing certain transaction costs like shipping and handling. Rather, the product would be stored in StockX's climate-controlled secure location (or vault), to be claimed at any time by the holder of the NFT, at which time the NFT is "removed" from circulation.

The Vault NFTs bear the image of the product in question. In the case of Nike product, that includes the company's name and logos as they appear on its sneakers.

Nike's Complaint:

Nike filed a complaint against StockX in the Southern District of New York (New York City) for trademark infringement and related dilution and false origin claims, seeking a permanent injunction to stop further use of the Vault NFTs bearing Nike's name and logos as well as money damages.

Comments:

This case is likely to test the limits of the first sale and nominative fair use doctrines under trademark law. StockX has asserted these defenses in its answer.

Under those doctrines, there is room to lawfully use Nike's name and logos when reselling its product and to display those in images of the goods without first obtaining permission. For example, a user can post a picture of an item when selling it on a resale platform like Ebay, and refer to the name of the product, and not trigger any trademark infringement issue. StockX argues that its approach with the Vault NFT is equivalent to that.

But Nike has its own NFT and "virtual goods" plan in connection with its product. It argues that the Vault NFT is a different and wholly separate product from the associated physical good and as such violates Nike's trademark rights by taking advantage of its branding in the buying and selling of that digital product.

The case is pending and in the pre-trial discovery phase.

2. Miramax v. Tarantino

Facts:

Last year film writer and director Quentin Tarantino announced plans to publish and "auction" seven "exclusive scenes" from his original handwritten screenplay for the 1994 movie *Pulp Fiction* via NFTs. The NFTs were intended to contain a digital scan of portions of his original screenplay together with a book cover bearing "a static original drawing [] inspired by some element of [each] scene."

Miramax's Complaint:

Miramax filed a complaint against Tarantino in the Central District of California (Los Angeles) for breach of contract, copyright infringement, trademark infringement, and unfair competition. Miramax says that Tarantino assigned almost all of the rights to *Pulp Fiction* to it, reserving only a very limited set of rights "far too narrow" for him to mint the intended NFTs.

Comments:

At its core, this lawsuit concerns a contract dispute. The parties entered into a series of written agreements, all attached to Miramax's complaint, all well in advance of the advent of NFTs.

Tarantino is likely to rely primarily upon language in the Reserved Rights provisions of the parties' contract reserving for him the right to "print publication [] including, without limitation, screenplay publication [] in audio and electronic formats, as applicable." He has also asserted various affirmative defenses in his answer, including fair use and First Amendment, that may impact Miramax's copyright and trademark infringement claims.

The case is pending and in the pre-trial discovery phase. A full-day mediation recently conducted by the parties failed to resolve the matter.

3. Lil Yachty v. Opulous

Facts:

Opulous (a foreign entity) announced a plan via extensive marketing and promotional efforts consisting of, among other things, press releases and social media and website posts, to launch a series of exclusive music "copyright-backed" Binance NFTs with "major artists – led by Lil Yachty." It employed the artist's (trademarked stage) name, image and likeness to do so. Following these efforts, Opulous reportedly raised $6.5 million in investment funding.

Lil Yachty's Complaint:

Lil Yachty filed a complaint against Opulous and related parties in the Central District of California for trademark infringement, unfair competition, and violations of the artist's right of publicity. He claims that he never gave permission to Opulous to use his name, image or likeness, or to trade in his copyrights or goodwill, to sell NFTs.

Comments:

There either is or is not an agreement of some kind between the parties. The nature and scope of any such agreement will be the crux of the matter.

4. Hermès v. Rothschild

Facts:

Conceptual artist or "digital speculator" (depending on who's talking) Mason Rothschild (a/k/a Sonny Alexander Estival) minted and marketed "MetaBirkins" NFTs, so-called because they feature the images of fashion designer Hermès famed Birkin bags together with certain graphic additions or flourishes. In the analog world, a genuine Birkin bag can fetch anywhere from $9,000 to half a million dollars. Rothschild apparently readily acknowledged that he was seeking to swap out Hermes "real life" rights for "virtual rights" and trying to "create the same kind of illusion [of value] that the Birkin bag has in real life as a digital commodity." He has reportedly sold over $1 million in MetaBirkins NFTs.

Hermès' Complaint:

Hermès filed a complaint (amended once) against the artist for trademark infringement, false designation of origin, trademark dilution, cybersquatting and injury to business reputation. The foundational claim is that the MetaBirkins NFTs are "fake Hermès products in the metaverse" that consumers could get confused and believe are real Hermès products.

Comments:

Rothschild responded to the complaint against him with a motion to dismiss, asserting that his MetaBirkins works were commentary on the "cruelty inherent in Hermes' manufacture of its ultra-expensive leather handbags" and therefore protected by the First Amendment and the fair use doctrine. He also argued that his work "does not lose its First Amendment protection just because he sells it" or uses NFTs to authenticate it. Rothschild maintained that his liability if any hinged on the test set forth in *Rogers v. Grimaldi*, 875 F.2d 994, 998-99 (2d Cir. 1989) and *Cliffs Notes v. Bantam Doubleday*, 886 F.2d 490, 494 (2d Cir. 1989).

"In deciding the reach of the Lanham Act in any case where an expressive work is alleged to infringe a trademark," the court wrote in the latter case, "it is appropriate to weigh the public interest in free expression against the public interest in avoiding consumer confusion." This balancing test is often called the "Rogers test" because of its origin in Ginger Rogers' failed attempt to enjoin Federico Fellini's use of the film title "Ginger and Fred" in the former case. Like the *Cliffs Notes* court, the *Rogers* court endorsed the use of a balancing test when First Amendment concerns are implicated: "We believe that in general the [Lanham] Act should be construed to apply to artistic works only where the public interest in avoiding consumer confusion outweighs the public interest in free expression."

The motion to dismiss presented a matter of first impression, and this past May, U.S. District Judge Jed Rakoff denied that motion in a one-page order with the promise that "the Court will issue an opinion in due course setting forth the reasons for this ruling." The court issued its 20-page opinion a few days later.

Notably, the court concluded that "the *Rogers* test applies, at least in part, to the trademark infringement analysis of Rothschild's uses of MetaBirkins" and that Rothschild's "trademark-using speech must be treated as noncommercial." Judge Rakoff adopted Rothschild's view that the *Rogers* test "is not inapplicable simply because [he] sells the images – the movie studio defendant in Rogers sold the film at issue. [Citation omitted.] Neither does Rothschild's use of NFTs to authenticate the images change the application of *Rogers*: Because NFTs are simply code pointing to where a digital image is located and authenticating the image, using NFTs to authenticate an image and allow for traceable subsequent resale and transfer does not make the image a commodity without First Amendment protection any more than selling numbered copies of physical paintings would make the paintings commodities for purposes of *Rogers*." An important footnote follows this quote, however, suggesting that "virtually wearable" bags bearing the "MetaBirkins" mark might infringe Hermès' rights.

Judge Rakoff ultimately declined to grant the motion, finding that "the amended complaint contains sufficient factual allegations that the use of the [Hermès] trademark is not artistically relevant and that the use of the trademark is explicitly misleading as to the source or content of the work." The court concluded it could "not resolve these factual disputes at the motion to dismiss stage."

The case is pending and in the pre-trial discovery phase.

5. <u>Dapper Labs Securities Class Action</u>

<u>Facts</u>:

Blockchain-focused technology company Dapper Labs created the NBA Top Shot platform. NBA Top Shot allows users to purchase and sell NFTs associated with specific NBA video clips called "NBA Top Shot Moments." The NBA Top Shot Moments consist of video clips of NBA game highlights. The NFTs exist on Dapper Labs' proprietary "Flow" blockchain.

NBA Top Shot sells three categories of "NBA Top Shot Moments," with prices based on the rarity of the clips. Individuals can buy and sell NBA Top Shot Moments in the secondary market, and the sales take place on the Top Shot platform, with Dapper Labs receiving a 5% transaction fee on all such sales as well as a "cash-out" fee upon a user exiting the Dapper "wallet." Since its inception, NBA Top Shot has sold in excess of $500 million of these NFTs.

<u>Class Action Complaint</u>:

In May of last year, a reputable class action firm filed a class action complaint against Dapper Labs and its founder/CEO in New York County Supreme Court, removed to the

Southern District of New York, for violations of federal securities law. The since-amended complaint alleges that the NFTs in question are "securities" within the meaning of the federal securities laws, i.e., "an investment of money in a common enterprise with a reasonable expectation of profits to be derived from the efforts of others," and that therefore Dapper was required to register them with the Securities and Exchange Commission.

Comments:

While this litigation does not address an intellectual property challenge, it raises the issue of under what circumstances NFTs might be considered securities such that they must be registered with the SEC. If the court determines that the NFTs in question are securities, Dapper Labs will have to either go through the registration process or verify that purchasers were "accredited investors."

Dapper's motion to dismiss the complaint against it is pending. Interestingly, in its motion, Dapper likens Top Shots to collectible playing cards.

6. Yuga v. Ripps / Bored Ape Yacht Club

Facts:

Yuga Labs is the entity behind the NFT project Bored Ape Yacht Club. BAYC is an NFT collection of 10,000 profile pictures, each portraying a Bored Ape wearing different costumes and accessories. In a little over a year, it emerged as a multi-billion-dollar business. Some of that business was no doubt driven by celebrity "buyers" like Madonna, Justin Bieber, Jimmy Fallon, Snoop Dogg, Serena Williams, Eminem and Shaquille O'Neal.

Ryder Ripps is a self-labelled "conceptual artist" who appeared on the Forbes' "30 Under 30" list several years ago. In May of this year, Ripps launched his own NFT project titled RR/BAYC. According to the official website, the collection "uses satire and appropriation to protest and educate people regarding The Bored Ape Yacht Club and the framework of NFTs."

Yuga Labs' Complaint:

Yuga Labs filed a complaint against Ripps in the Central District of California for trademark infringement, false designation of origin, cybersquatting, and conversion, on the basis that Ripps created and sold NFTs bearing "the very same trademarks that Yuga Labs uses to promote and sell authentic BAYC NFTs."

Comment:

Although this case pits an NFT proprietor against another NFT proprietor, it is likely to line up much like the MetaBirkins case. Ripps responded to the complaint with an anti-SLAPP motion under California law.

7. **Roc-A-Fella Records v. Dash**

Facts:

Damon Dash attempted to mint Jay-Z's debut album *Reasonable Doubt* as an NFT and to auction it to the highest bidder. Dash promoted this intended auction as one that would "provide ownership of the album's copyright, transferring the rights to all future revenue generated by the album from Damon Dash to the auction winner." The problem for Dash: He did not actually own the copyright to *Reasonable Doubt* (although he does apparently own a one-third interest in Roc-A-Fella Records, Jay-Z's record label and the owner of the copyright in and to the album).

Roc-A-Fella's Complaint:

Roc-A-Fella filed a complaint against Dash in the Southern District of New York for copyright infringement, and immediately moved for a temporary restraining order and preliminary injunction blocking any sale of the proposed NFT. The parties subsequently stipulated to entry of a restraining order. Dash responded to the complaint with an answer and countercomplaint against Roc-A-Fella for declaratory judgment on RAF's corporate governance issues.

In June of this year, the parties reached a settlement of the matter and judgment by joint stipulation was entered in the case. Dash acknowledged that he had no right to sell any interest in *Reasonable Doubt* (although he maintained whatever right he had to dispose of his interest in Roc-A-Fella Records). Both sides dismissed their respective claims without prejudice.

Comments:

The case was one of the first to raise issues concerning underlying rights (in this case, copyright) to the intellectual property embodied in the NFT.