

Navigating NFT Brand Management Risks And Rewards

By **David Ervin, Kayvan Ghaffari and Carissa Wilson** (April 30, 2021, 5:44 PM EDT)

Interest in nonfungible tokens and blockchain technology has erupted in recent months including newscasts, legal and tech websites, and social media platforms.

As with all things new, experts and commentators have been quick to question the staying power of NFTs, claiming these novel assets are in fact nothing more than a kink among techies and journalists that is likely to burn hot but fast.

However, substantial investment by major brands continues to suggest real value in buying, selling and simply using NFTs — perhaps even more so in the brand management and retail spaces than in the more often discussed digital art world.

NFTs are not limited to their functions as digital trading cards or digital art provenances.

Instead, they can be used in many ways and can even be associated with physical merchandise, creating new and potentially longer-lasting implications for this novel technology as employed by traditional retailers.

Brand and business owners should take note of broader NFT opportunities and corresponding risks, particularly with respect to trademark, licensing, anti-counterfeiting and advertising law.

NFTs and Trademarks

Brand and business owners may be able to generate new value — in the form of brand recognition, business goodwill or even licensing revenue — by creating and protecting NFT trademarks.

The creation of an NFT trademark does not involve trademarking the NFT or digital information file itself. Instead, the practice involves trademarking a brand associated with the offering of an NFT.

To be accepted by the U.S. Patent and Trademark Office, a trademark must be: (1) distinctive, (2) nonfunctional and (3) used in commerce.



David Ervin



Kayvan Ghaffari



Carissa Wilson

In the case of an NFT trademark, the alleged use in commerce is the offering of, or intent to offer, an NFT.

Notably, a bona fide intention to use the mark in commerce in the future can satisfy prong three when the applicant makes actual use within six months.

Potential NFT-based trademark activities fall into at least four major categories. Each of these four categories is discussed below.

First, brand and business owners might license their trademarks to NFT creators in exchange for royalties.

This could be done in much the same way traditional trademark holders license marks to clothing manufacturers and so on. It would require negotiating usage and royalty terms to be reflected in a trademark licensing agreement, a type of merchandise agreement.

This licensing practice may, itself, create a new revenue stream demonstrating alternative business value derivable from NFTs.

Second, brand and business owners might use the offering of an NFT that includes a brand name or other potential trademark to become the "first substantial good faith user" of the mark.

Such users may be awarded common law trademark protection, at least in their particular geographic area of use, even against subsequent registered users.[1]

Offering an NFT is a particularly valuable substantial use, since the information on the blockchain will serve as evidence of the use and its earliest date.

The question, however, is the geographic area in which a court would find the NFT-based internet use to exist. Potentially, the relevant geographic area would be based on the locations of purchasers, which might prove too "sporadic and/or de minimis in a given area" to justify regional protection.[2]

Third, brand and business owners might apply for a new trademark to be used in their NFT business. For example, the Chainsmokers, a popular music group, has filed a trademark application for the NFT-focused mark Blockchainsmokers.

The creation and protection of new trademarks contributes new intellectual property assets to an owner's portfolio that can likely be monetized.

Fourth, brand and business owners might seek to expand their use of an existing trademark by filing a new application, ensuring protection of the mark in additional trademark classes. The USPTO divides trademarks into 45 different classes of products and services. A mark registered in one class does not infringe on a mark registered in a separate class. Furthermore, once an application is filed, it is not possible to add new classes without refiling.

Thus, holders of existing trademarks in categories dealing with, for instance, luxury goods may need to file new applications in NFT-appropriate categories like advertising and business services — Class 35 — or science and technology services — Class 42.

Otherwise, it is possible an NFT-based use of an existing registered mark would not be entitled to trademark protection.

Trademark infringement risks also exist in this area. To support a trademark infringement claim in court, a plaintiff must prove (1) that it owns a valid mark; (2) that it has priority, i.e., its rights in the mark are senior; and (3) that the alleged infringer's mark is likely to cause confusion in the minds of consumers about the source of goods or services offered under the mark.

Trademark infringement in the NFT context might play out in multiple ways. First, if a business with an established mark in a category like clothing — Class 25 — begins to use the mark in an NFT, that use might well infringe some other similar mark already registered in Class 35 or 42.

Alternatively, if an NFT creator generates an NFT that happens to contain a third-party mark, that person could be subject to trademark infringement liability. Under either circumstance, the newness of NFTs to judges and litigators may produce costly litigation uncertainty where infringement claims are actually filed and litigated.

These benefits and risks should be carefully considered by businesses seeking to expand existing uses of their marks or to create new marks that might contain protected third-party intellectual property.

NFTs and Counterfeiting

Importantly for brand and business owners as well as consumers, NFTs have potential usefulness not only in association with digital images but also for physical products. According to a Gucci executive, NFTs for physical luxury goods are inevitable, which would open up a new field of NFT uses.[3]

In addition to their purchase value as mere novelties for brand-loyal consumers, NFTs may be useful anti-counterfeiting devices. In the context of digital art, an NFT may be seen to have limited value where the associated artwork exists in hundreds of perfectly identical copies.

In the world of physical goods, however, consumers are likely already aware that more than one of a particular product is being sold. What is really desired in most cases is merely source verification. Notably, LVMH Group is reportedly already using the AURA blockchain to allow customers to trace the authenticity of luxury goods using NFT-related technology.[4]

On the other hand, uncurtailed NFT abuse may enhance counterfeiting risks. If NFTs are minted that contain phony information, consumers could be misled as to the nature or value of their NFT purchases. If NFTs for physical luxury goods are popularized, as Gucci suggests, NFTs could contribute substantially to the trade in knockoffs, as where an unauthorized NFT is used in an effort to demonstrate the authenticity of a fake product.

To minimize counterfeiting and ensure that NFTs remain a net positive in this area, retailers should carefully consider the manner in which they will employ NFTs. Specifically, retailers could record NFT-associated goods on a specific, exclusive blockchain.

The market could then be informed that only items listed on this particular blockchain are authentic. Additionally, retailers could exploit NFT date stamps and inform the market that only goods created between certain dates are authentic. This added assurance of authenticity may be found to increase

demand—and even prices—for NFT-associated goods.

Brand and business owners should consider the usefulness of NFTs in proving the authenticity of physical goods and potentially driving prices. However, corresponding risks should also be considered and countered, including the risk of future consumer safety regulation if NFTs are found to increase, rather than decrease, counterfeiting or trade in knockoffs.

NFTs and False Advertising

Brand and business owners and other parties who sell NFTs should also be aware of false advertising, a doctrine closely related to trademark and anti-counterfeiting law. Because of the technological and legal complexities of NFTs, it may be unclear to consumers exactly what they are purchasing and what kind of rights they will obtain through the purchase of an NFT.

This creates a risk of false advertising liability for those engaged in NFT sales.

Under the Lanham Act, NFT purchasers might have a claim for false advertising if they can show: (1) the seller made false or misleading statements as to the NFT products; (2) actual deception or a tendency to deceive a substantial portion of the intended audience; (3) the deception is material; (4) the advertised NFT goods travel in interstate commerce; and (5) a likelihood of injury to the plaintiff.

To preempt these kinds of claims, brand and business owners who sell NFTs should be extremely clear about the ownership contours of each transaction — for example, that an NFT purchase does not convey the copyright for the associated digital image, or that a particular physical product is one of many, each sold with its own NFT.

Some NFT platforms, like the National Basketball Association's NBA Top Shot, have already acted to prevent false advertising liability by promulgating NFT license templates that carefully distinguish the NFT token from the associated digital artwork or other content.[5]

These types of templates may be useful to NFT platform owners and sellers in preventing false advertising liability and could likely be adapted for use in the physical retail sector.

Conclusion

While the lasting value of NFTs in some contexts — like high-price digital art — may be uncertain, new uses for this novel technology seem sure to arise.

Particularly in the brand management and elite retail contexts, NFTs may create value by increasing brand recognition, business goodwill and licensing revenue, or may operate as anti-counterfeiting devices verifying product authenticity.

However, parallel risks of trademark infringement, increased counterfeiting, and false advertising liability also exist.

Brand and business owners seeking to utilize NFTs should consider not just the standard opportunities and risks contemplated by mainstream media but also creative applications of NFT technology that may be longer-lasting and of greater relevance to a larger number of consumers.

David Ervin is a partner, Kayvan M. Ghaffari is counsel and Carissa Wilson is an associate at Crowell & Moring LLP.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] E.g., *Dudley v. HealthSource Chiropractic, Inc.*, 883 F. Supp. 2d 377, 394 (W.D.N.Y. 2012) ("Common law trademark rights only extend to the territories in which the mark's adopter sells its products, renders its services, establishes recognition of its mark, or draws its trade.").

[2] Jerome Gilson & Anne Gilson LaLonde, *Proving Ownership Online...And Keeping It: The Internet's Impact on Trademark Use and Coexistence* 15 (2014), available at https://www.brinksgilson.com/files/gilson_on_trademarks_article_2014.pdf.

[3] Marc Bain, *NFTs for Fashion are Inevitable*, Quartz (Mar. 19, 2021), <https://qz.com/1986615/nfts-for-fashion-in-the-real-and-virtual-worlds-are-inevitable/>.

[4] Ian Allison, *Louis Vuitton Owner LVMH is Launching a Blockchain to Track Luxury Goods*, Coindesk (Mar. 26, 2019), <https://www.coindesk.com/louis-vuitton-owner-lvmh-is-launching-a-blockchain-to-track-luxury-goods>.

[5] Ghaith Mahmood, *NFTs: What Are You Buying And What Do You Actually Own?*, The Fashion Law (Mar. 18, 2021), <https://www.thefashionlaw.com/nfts-what-are-you-buying-and-what-do-you-actually-own/>.