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BLOG

NFTs: The Tools of the Metaverse Present Unique Opportunities and Commensurate Business and Legal Risks

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It’s no secret that scarcity (real or perceived) can drive demand, remember beanie babies?

In the last year, there has been a surge of Non-Fungible Token (NFT) trading volume, much attributable to popular projects with limited numbers such as CryptoPunks, Bored Ape Yacht Club, and Meebits, which are essentially collections of unique images whose ownership is proven by an NFT.[1]

Last March, Mike Winkelmann (known as Beeple) sold an NFT of his work for $69 million at Christie’s.[2]

In August, someone even paid $1.3 million for a collectible JPEG of a cartoon rock.[3] The original source for the image confirms on their website, “These virtual rocks serve NO PURPOSE beyond being able to be bought and sold, and giving you a strong sense of pride in being an owner of 1 of the only 100 rocks in the game :).”[4]

While this all may seem silly, NFTs are not a fad or transient internet phenomenon. They may enable fads that lead to asset bubbles, but NFTs are simply certificates that prove ownership of an asset—which can be anything from clipart of a rock to a patent—and are here to stay.

In fact, NFTs are the key to understanding how money will work in the Metaverse. Cryptocurrencies like Bitcoin and Ethereum will be the money used to purchase the *stuff* that makes up the Metaverse—digital assets in the form of NFTs.

These NFTs can represent anything from a designer handbag for your avatar to a plot of virtual real estate.[5] Twitter even recently introduced a feature allowing users to signal they own their profile picture as an NFT.[6]

Scotch distiller Glenfiddich recently used NFTs to sell a collection of super-rare, 46-year-old bottles of whiskey for $18,000 each—close to what the bottles would have gone for in a traditional sale.[7] The actual NFT is an artistic impression of the bottle that allows the owner to show it off online, and acts as a counterfeit proof of ownership.[8] The bottles will stay in the custody of the company until the customer wants to claim it, at which point the NFT is “burned” or destroyed.[9]

LUXURY GOODS

Many luxury brands have announced their plans to offer digital versions of their products to consumers hoping to show off in the Metaverse.[10]

Gucci and Nike have partnered with Roblox—a platform where users can create games and geographies for others—to create The Gucci Garden and Nikeland.[11] A Gucci bag was recently sold on Roblox for $4,115, which is more expensive than the bag's real-world price.[12]

Tommy Hilfiger announced a partnership with a marketing agency to focus on "v-commerce."[13] Burberry released playable NFT creations in the virtual world *Blanko's Block Party* by Mythical Games.[14] Morgan Stanley analysts estimate the market for virtual luxury goods could reach $50 billion by 2030.[15]

Dolce & Gabbana intertwined virtual and real-life fashion at a show in September, unveiling a nine-look collection—four virtual-only designs and five including a real-world garment—attached to NFTs that sold for $5.7 million.[16]

PlatformE is a Portuguese tech provider that has helped conglomerates Kering and LVMH deploy 3D renderings of their brands' products.[17] PlatformE's co-founder, Gonçalo Cruz, views the Metaverse as a way to help the fashion industry avoid problems such as overproduction and over-inventory, which lead to discounts that devalue brands.[18] Cruz posits that training shoppers to start online instead of in-store—using avatars with sizing built in—could allow brands to only produce the stock that has already been sold instead of filling stores worldwide.[19]

Other upsides exist as well—brands can bring old designs back with ease, and NFT contracts will enable them to receive royalty fees or revenue shares on future transactions when pieces change hands.[20]

VIRTUAL REAL ESTATE

Real estate in the Metaverse is booming.[21] NFTs can be used to denote ownership and act as a key to control access to real estate in Metaverse platforms such as Decentraland and The Sandbox.[22] As of Wednesday, January 5, 2022, the cheapest parcel of land in The Sandbox was over $14,000.[23] In contrast, the cheapest parcel of land in Decentraland was over $13,000.[24]

Digital real estate investment funds Republic Realm and the Metaverse Group purchased NFT plots last year in Decentraland for $913,000 and $2,428,740, respectively.[25] PricewaterhousCoopers (PwC) recently bought a plot of land for an undisclosed amount to join Adidas and other brands on the platform.[26]

Total sales of NFTs have also surged in The Sandbox, populated by the likes of deadmau5, Richie Hawtin, The Walking Dead, The Smurfs, and SnoopDogg among over 160 other brands.[27] The daily trading volume on the platform reached $180 million in December after someone paid almost $500,000 for a piece of virtual land in the form of an NFT next to Snoop's own plot.[28]

For a glimpse into how the Metaverse is already supplementing the real world, look no further than one of the world's largest sporting events—the Australian Open.[29] This year, the tournament has entered both the Metaverse and NFT market by allowing visitors to observe the stadium, explore restaurants, and watch tennis matches in Decentraland amid concerns over the omicron variant of Covid-19.[30] Additionally, the tournament is releasing a collection of 6,776 NFTs called "Art Ball NFTs" each of which correspond to a winning shot from the 2022 championship.[31] Resale of the Art Balls released in the first two weeks of the tournament generated almost $4 million in trading value.[32] Electronics giant Samsung also recently announced Samsung 837x, its new Metaverse experience in the virtual world which will enable clients to virtually attend quests or live music events.[33] Users will also have the ability to earn NFT badges and limited-supply Samsung wearables for their avatars.[34] Samsung and the Australian Open join Sotheby's as major brands to open up a replica of a real-world property in Decentraland.[35]

TAKEAWAYS

NFTs exploded into the national conversation in 2021 due to the exorbitant prices that certain pieces fetched. While any one NFT collection may be a bubble doomed to burst, the technology allowing ownership of any unique asset to be verified by the blockchain will certainly have its uses going forward as the Metaverse takes shape. NFTs allow users to own their virtual items independently of any developer whose platform they are using, protecting their rights in any work created or item purchased. Businesses looking to grow may want to enter the Metaverse to stay ahead of the curve, as early adopters can reach a new crop of virtual consumers before the competition, building a foothold in the virtual economy. With less overhead for a virtual store and low production costs for virtual goods, businesses may be able to improve their margins while expanding their customer base by establishing a virtual presence.

BUSINESS & LEGAL RISKS

The pace of adoption is breathtaking and has far outpaced the ability of traditional legal approaches to keep up. The risks are significant. As we wrote, business risks include disaffected customers. The legal risks are significant as well. Because NFTs are classified as property instead of securities, wash trading is rampant in many NFT markets. [36] NFTs and tokens present other legal risks, too, ranging from securities to copyright. Traditional real estate is governed by established state, local, and national laws. There is no similar framework for real estate transactions in the Metaverse.

Our attorneys proactively follow and advise on trends in this quickly evolving space. We invite all those interested in recent developments to sign up to receive emails with links to new posts by clicking here.

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[21] Holmes, *supra* note 5.

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