

Jurisdictional briefing, US: Don't forget the NFTs: IP due diligence for emerging technologies

Michelle Ciotola and David Kincaid of Cantor Colburn evaluate the expectations for how the USPTO will handle IP due diligence for an exciting, if not emerging, technology.

NFTs, or non-fungible tokens, are one of the hottest trends in tech over the past year. NFTs use blockchain technology, such as the Ethereum blockchain, to record transfers of unique assets while providing proof of ownership. Non-fungibility means that an NFT is unique and cannot be replaced with an equivalent item, unlike bitcoin or currency that can be replaced with other bitcoin or currency. When an NFT is generated (or "minted"), a unique digital fingerprint is created and recorded to the blockchain, which acts as a public digital ledger to record transactions, such as a transfer of an NFT and/or a transfer of an underlying asset tied to the NFT. One example use case for NFTs is to transfer IP rights or ownership.

As NFTs are developed, acquired, and licensed by companies, the landscape of commercial transactions involving intellectual property will change. In the case of transfers, mergers, acquisitions, bankruptcies, or other transactions, an accurate assessment and allocation of intellectual property assets is crucial. NFTs will add a new and complicated layer to due diligence – in terms of both tracking and transferring.

It is important for the parties transacting NFTs to understand their rights, especially when conducting IP due diligence. Although NFTs claim to provide proof of ownership, such ownership is usually of the NFT itself and may not transfer to the underlying asset. It can be unclear what rights are being



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transferred when an NFT passes from one party to another, especially when IP rights are concerned. Consider, for example, a piece of digital artwork or a digital sports trading card. The creator of such an asset may wish to mint an NFT for the asset, and the NFT can then be sold. In such cases, the party acquiring the NFT acquires ownership of the NFT but may receive only a limited license to own and use the NFT without ownership rights in the underlying work. The party acquiring a digital trading card as an NFT may be licensed to possess and re-sell the digital trading card but may not be authorized to make copies of the digital trading card, as these rights may be retained by the original copyright owner.

When evaluating NFTs in the context of IP due diligence, it is important to determine the scope of the granted license that accompanies an NFT. The terms of the limited licenses conveyed with NFTs are set by the marketplaces on which the NFTs are listed for sale and/or by the creator. Each marketplace can include its own license terms and may differ from one marketplace to another. In some cases, however, the party minting the NFT may not be the original creator, and as such, may only have limited rights themselves. It is therefore important to understand what rights are being conveyed when an NFT is transferred.

Yet another aspect to consider when evaluating NFTs involves how NFTs are used to facilitate a more conventional asset transfer, such as a

transfer of tangible or intellectual property. It is conceivable that a company and its assets may be sold as an NFT, similar to the recent sale of real estate. In February, a Florida home was auctioned off as an NFT and sold for US \$653,000 of ether (ETH – the cryptocurrency on the Ethereum Network). The property rights of the house were minted as NFT. Ownership in the home was transferred from the seller to a limited liability company (LLC), which was then transferred to the winner of the auction. This approach claims to reduce transaction costs and speed up transactions. Where the transfer of an LLC involves more than just the physical property, but intellectual property as well, more questions are raised regarding how the transfers can be tracked and recorded. It is important to investigate the underlying transfer of trademark rights to the LLC to ensure that the transferring LLC has clear title, and that all rights in the trademarks are transferred, including the goodwill.

Even where there is a clear record of ownership of NFT assets, there may be questions about the property transfer of the same. For example, how the transfer of these assets will be tracked and handled by the United States Patent and Trademark Office (USPTO) or the U.S. Copyright Office, where the validity of a transfer hinges on satisfying certain criteria. In the case of a trademark, the assignment must be in writing and duly executed and must include the goodwill of the business in which the mark is used. Conceivably, a transfer may occur using NFTs in place of conventional paper assignments. How such transfers will be treated by governments and courts remains uncertain. For example, how will the USPTO, courts, or foreign jurisdictions treat such a transfer absent conventional documentation – can an NFT transfer replace conventional paper assignments? These authors believe the answer is no, at least in the short term.

But with this in mind, we wonder how will courts handle disputes involving the transfer of assets via NFT? Where there is a disagreement between a conventional transfer and a transfer on the blockchain, how will it be resolved? How can it be resolved? Even assuming a court rules on the side of an assignee of a conventional assignment, how will this be enforced where the recorded owner on the blockchain is unknown or outside the jurisdiction of the United States?

While NFTs remain an exciting, if not emerging, technology, their use poses challenges that should be



Résumés

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Michelle Ciotola counsels clients on protecting and enforcing their trademark, trade dress, copyright, and related IP rights, including unfair competition, Internet, advertising, and promotions law. She counsels clients in developing and exploiting their trademark portfolios, including clearance; prosecution; and identifying important overseas jurisdiction and filing or coordinating with local counsel overseas. Michelle develops strategies for the enforcement of her clients' IP rights, including preparing demand letters, negotiating settlement agreements, handling opposition and cancellation actions before the U.S. Trademark Trial and Appeal Board, and coordinating and overseeing litigation with local counsel around the world. She also develops strategies for enforcement of her clients' intellectual property rights online, including handling Uniform Domain Name Dispute Resolution Policy proceedings. Michelle attends and speaks at International Trademark Association (INTA), MARQUES, European Communities Trade Mark Association (ECTA) and the Asociacion InterAmericana de la Propriedad Intelectual (ASIPI).

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David Kincaid concentrates on assisting clients in solving IP problems and protecting their investments in product development and has significant experience protecting inventions related to or incorporating artificial intelligence (AI), augmented reality (AR), virtual reality (VR), cloud computing, and other emerging technologies. David has prepared and prosecuted patent applications about: artificial neural network architectures and algorithms for image processing, natural language processing, and the like across various industries; reinforcement learning for autonomous driving; AR for 3D data visualization; VR user feedback systems; and cloud architecture and infrastructure management systems. David is a thought leader in the AI technology space being active in the Intellectual Property Owners Association committees on Software Related Inventions and AI & New Emerging Technologies.

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considered when evaluating these assets, especially in the context of IP due diligence. It remains good practice to support any blockchain-based transactions with conventional paper documentation (e.g., assignments) to help avoid any uncertainty with how such digital transfers may be treated in the future.

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