

# A Legal Practitioner's Guide to NFTs, Digital Advertising and Media

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## A Digital (and Physical) Branding Phenomenon

In 2021, non-fungible tokens (NFTs) generated overall sales of close to \$25 billion<sup>1</sup> and became one of the year's most defining cultural phenomena. This trend has continued with NFT sales topping \$2 billion in the first quarter of 2022.<sup>2</sup>

In an effort to engage audiences and produce secondary revenue streams, brands—in sectors ranging from fashion to sports, alcohol to art, music to beauty—melded visual media, blockchain technology and e-commerce to create and market new NFT-based digital brand campaigns for everything from toilet paper<sup>3</sup> to tacos.<sup>4</sup> If the first months of 2022 are any indication, advertisers' interest in the digital sphere shows no signs of waning, with brands using NFTs to market digital campaigns from Puppy Bowl trading cards<sup>5</sup> to lifetime music

<sup>1</sup> Elizabeth Howcroft, *NFT Sales Hit \$25 Billion in 2021, But Growth Shows Signs of Slowing*, Reuters (Jan. 11, 2022, 10:50 a.m. EST), <https://www.reuters.com/markets/europe/nft-sales-hit-25-billion-2021-growth-shows-signs-slowng-2022-01-10>.

<sup>2</sup> Robert Frank, *NFTS Sales Top \$2 Billion in First Quarter, With Twice as Many Buyers as Sellers*, CNBC (April 13, 2022), <https://www.cnn.com/2021/04/13/nft-sales-top-2-billion-in-first-quarter-with-interest-from-newcomers.html>.

<sup>3</sup> <https://news.pg.com/news-releases/news-details/2021/Charmin-Rolls-Out-First-Ever-NFTP/default.aspx>.

<sup>4</sup> <https://rarible.com/tacobell/sale>.

<sup>5</sup> *Puppy Bowl*, Discovery.com, <https://www.discovery.com/shows/puppy-bowl/collect> (last accessed Jan. 15, 2022).

festival passes<sup>6</sup> to private eating club memberships.<sup>7</sup> For many brands, NFT initiatives are their first foray into the emerging metaverse.

An NFT may carry ownership rights to a digital media file, such as an image<sup>8</sup> or a video,<sup>9</sup> and may sometimes include rights to physical/consumptive items, such as a rare cask of sherry<sup>10</sup> or a time share in a parcel of real estate.<sup>11</sup> Brand offerings have taken both forms. NFTs that provide access rights to only digital media have been more common, with name brands such as Marvel,<sup>12</sup> Disney,<sup>13</sup> ViacomCBS,<sup>14</sup> Macy's<sup>15</sup> and GAP<sup>16</sup> all entering the NFT market in this manner. However, NFTs that offer both digital media file access and the right to a physical/consumptive item have become more popular. For example, Mattel launched an NFT auction for a Barbie-Balmain collaboration featuring unique Barbie avatars adorned in Balmain-designed outfits where the highest bidders also received a physical set of Barbie-sized Balmain pieces,<sup>17</sup> and Levi's promoted a contest in France featuring a prize that consisted of a pair of limited-edition recyclable 501 Originals to be accompanied by an NFT that allows for free jean repair until 2027.<sup>18</sup>

6 Dimitar Dzhondzhorov, *Coachella and FTX to Sell Lifetime Festival Passes as Solana-Based NFTs*, CryptoPotato (Feb. 5, 2022), <https://cryptopotato.com/coachella-and-ftx-to-sell-lifetime-festival-passes-as-solana-based-nfts/>.

7 Luke Fortney, *We Regret to Inform You the World's 'First NFT Restaurant' Will Be in New York*, Eater New York (Jan. 13, 2022), <https://ny.eater.com/2022/1/13/22880787/worlds-first-nft-restaurant-flyfish-club-opening-nyc>.

8 Scott Reyburn, *JPG File Sells for \$69 Million, as 'NFT Mania' Gathers Pace*, NY Times (Nov. 3, 2021), <https://www.nytimes.com/2021/03/11/arts/design/nft-auction-christies-beeple.html>.

9 Jacob Kastrenakes, *Grimes Sold \$6 Million Worth of Digital Art as NFTs*, The Verge (March 1, 2021), <https://www.theverge.com/2021/3/1/22308075/grimes-nft-6-million-sales-nifty-gateway-warnymph>.

10 Kat Bein, *Rare Aged Macallan Sherry & Trevor Jones NFT Art Package Sells for \$2.3 Million*, Gotham (Oct. 28, 2021), <https://gothamag.com/macallan-sherry-trevor-jones-nft-metacask>.

11 Chris Jones, *With This NFT, You Could Own Part of a Glamping Resort Near Bali*, CoinTelegraph (July 13, 2021), <https://cointelegraph.com/news/with-this-nft-you-could-own-part-of-a-glamping-resort-near-bali>.

12 Press Release, *First-Ever Marvel Digital Comic Collectibles Arrive on VeVe*, Marvel.com (Aug. 18, 2021), <https://www.marvel.com/articles/gear/first-ever-marvel-digital-comic-collectibles-nft-veve>.

13 Lilit Chichyan, *Mickey Mouse NFT Collection Announced by Disney & VeVe*, CoinChapter (Dec. 23, 2021), <https://coinchapter.com/mickey-mouse-nft-collection-announced-by-disney-veve/>.

14 Press Release, *ViacomCBS Enters Strategic NFT Partnership with RECUR*, ViacomCBS.com (Oct. 13, 2021), <https://ir.viacomcbs.com/news-releases/news-release-details/viacomcbs-enters-strategic-nft-partnership-recur>.

15 <https://www.macys.com/social/macys-parade-nft/>.

16 <https://www.gap.com/nft/>.

17 Tora Northman, *Balmain, Barbie & the Blockchain*, HighSnobiety (Jan. 13, 2022), <https://www.highsnobiety.com/p/balmain-barbie-collection-nft/>.

18 Ann-Christine Diaz, *The Top 5 Creative Campaigns You Need to Know About Right Now*, AdAge (Jan. 10, 2022), <https://adage.com/article/special-report-creativity-top-5/top->

Alcohol brands have also adopted NFTs as a means to bring their previously "exclusive" cask auctions to the masses. Recent NFT sales have paired spirit-inspired digital artwork with physical bottles of booze: a limited edition Glenfiddich 1973 46-year-old single-malt scotch whisky,<sup>19</sup> a Hennessy8 cognac<sup>20</sup> and a 1991 Macallan cask of sherry.<sup>21</sup>

## New Consumer Connections, Revenue Streams, and Digital Frontiers

Advertisers have embraced NFTs as a new means of boosting both brand visibility and revenue. The consumer experience of participating in NFT "drops" and secondary market trading has opened new avenues for advertisers to deliver unique brand experiences, interact with and expand their customer base, and generate promotional excitement for an upcoming event or product launch. Additionally, many brands have used the sale of NFTs to generate secondary, often lucrative, revenue streams. For example, the NBA<sup>22</sup> and NFL<sup>23</sup> partnered with Dapper Labs to launch proprietary platforms on which to sell commemorative and collectible digital memorabilia, generating over \$500 million in gross sales,<sup>24</sup> and fashion label Dolce & Gabbana sold a nine-piece virtual collection for \$6 million.<sup>25</sup>

NFTs are also a key component of new advertising frontiers in the metaverse. While the technology underpinning the metaverse—and perhaps even the definition of the metaverse—is still evolving, brands have already begun to embrace the potential for new advertising opportunities, and many of these initiatives involve NFTs. Fashion houses Balenciaga, Gucci, Burberry and Louis Vuitton each recently put forth collections in the digital realm, offering options from virtual fashion shows<sup>26</sup> to haute couture digital wearables.<sup>27</sup> Athletic brands

[5-best-commercials-brand-ideas-january-10-2021/2392021](https://www.glenfiddich.com/us/explore/blockbar-nft/).

19 <https://www.glenfiddich.com/us/explore/blockbar-nft/>.

20 Amy Rosner, *Be the Only Person in the World With This Exclusive \$226k+ NFT*, Gotham (Jan. 10, 2022), <https://gothamag.com/hennessy-blockbar-nft>.

21 Gina Pace, *A Macallan Cask NFT Sold for \$2.3 Million*, Forbes (Oct. 31, 2021), <https://www.forbes.com/sites/ginapace/2021/10/31/a-macallan-cask-nft-sold-for-23-million-what-does-this-mean-for-whisky-collectors/>.

22 <https://nbatopshot.com/>.

23 <https://nfl.live-nfts.com/>.

24 Tim Levin, *NBA Top Shot is Booming*, Insider (April 24, 2021), <https://www.businessinsider.com/nba-top-shot-withdrawal-delays-growing-pains-2021-4>.

25 Dana Thomas, *Dolce & Gabbana Just Set a \$6 Million Record for Fashion NFTs*, NY Times (Oct. 4, 2021), <https://www.nytimes.com/2021/10/04/style/dolce-gabbana-nft.html>.

26 Anders Christian Madsen, *5 Things to Know About Balenciaga's Virtual Reality AW21 Show*, Vogue (Dec. 6, 2020), <https://www.vogue.co.uk/news/gallery/balenciaga-autumn-winter-2020>.

27 Colleen Barry, *Gucci Digitally Outfits Gen-Z in Metaverse Foray With Roblox*, AP News (June 9, 2021), <https://apnews.com/article/gucci-roblox-76339d10f139e9bd39761b>

Nike<sup>28</sup> and Adidas<sup>29</sup> have created online virtual worlds that allow consumers to interact with digital merchandise, purchase NFTs and engage with other branded content.

## Navigating Intellectual Property Rights

One of the primary considerations for brands seeking to enter the NFT market is the intellectual property (IP) rights involved in minting and distributing an NFT. For advertisers, the IP considerations can be reduced to two questions: (i) What rights do you control?; and (ii) How do you want to exercise those rights?

### 1. Brand Ownership of Underlying Rights

Prior to minting an NFT, a brand should first determine what rights it owns and the underlying media content that is linked to the NFT (NFT Media). This analysis will vary depending on the type of media involved (photo, video, interactive) and the rights (if any) the brand intends to confer to potential NFT purchasers, but it will generally follow a traditional analysis of copyright, trademark and right of publicity issues.<sup>30</sup>

### 2. Rights Given to the Purchaser

Once a brand has determined what rights it holds, it should then ask the following questions: (i) What rights does it want to confer on the purchaser/recipient?; (ii) What rights should it reserve?; and (iii) How should all this be messaged to the consumer? The answers to these questions will define the design and execution of the NFT promotion. Key best practices include the following.

#### a. Copyrights

Brands generally will want to explicitly restrict the rights conferred to the purchaser and grant only a limited license to display the NFT Media for personal use. It is important that consumers know that the purchase of an NFT *does not* give them the right to (i) reproduce the NFT Media, (ii) transform the NFT Media, (iii) create a derivative work based on the NFT Media or (iv) use the NFT Media in a commercial

endeavor. While such caveats may seem obvious to legal minds, they will definitely not be obvious to an average consumer. Accordingly, these restrictions should be clearly and conspicuously disclosed to purchasers.

#### b. Trademarks

Brands should determine whether and how they wish to use their marks in connection with NFTs. While inclusion of a mark may help raise visibility and brand awareness, it also brings an increased risk of misappropriation.<sup>31</sup> Brands that use their marks in connection with NFTs should be prepared to increase their monitoring of online marketplaces for potential downstream misuse of such marks.

#### c. Royalty Payments

Unlike in the physical world, where the secondary resale of an item does not benefit the original artist/designer/creator, the digital world has changed that paradigm. Thanks to coding built into smart contracts, digital creators can reap the rewards of the resale of their images used as NFT Media—potentially in perpetuity. However, it is important that brands make clear to consumers that the mere purchase or receipt of an NFT does not confer the right to participate in secondary market royalties when a future sale of the NFT or the NFT Media occurs. As this will likely not be intuitive to most consumers, it is incumbent upon the brands to message this clearly when selling NFTs.

#### d. Rights Termination

Brands should also consider the termination of any rights conferred to an NFT purchaser/recipient, especially if the NFT Media contains brand-related trademarks and copyrights. Brands may want the option to revoke user licenses if certain conditions are violated. This may be accomplished by including language to that effect in the purchaser terms of use. User rights may also be terminated through certain technical controls. For example, if the NFT Media is hosted on a cloud account controlled by the seller/brand, the seller/brand may retain the technical capability to delete, alter or otherwise disassociate the NFT Media from the NFT token.

## Choosing the Right Partners

The creation and sale of NFTs require brands to partner with third-party vendors. Because such affiliations can create additional

<sup>31</sup> See, e.g., *Hermès Int'l v. Rothschild*, 1:22-cv-00384 (S.D.N.Y.), in which Hermès sued digital artist Mason Rothschild asserting claims including federal trademark infringement and dilution for Rothschild's use of the Birkin mark in the unauthorized NFT collection MetaBirkins, and *Nike, Inc. v. StockX LLC*, 1:22-cv-00983 (S.D.N.Y.), in which Nike similarly sued StockX, an online resale platform, asserting claims of federal trademark infringement and dilution for StockX's sale of NFTs that included images of Nike sneakers.

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<sup>28</sup> *Into the Metaverse: Nike Creates 'NIKELAND' on Roblox*, Reuters (Nov. 18, 2021), <https://www.reuters.com/technology/into-metaverse-nike-creates-nikeland-roblox-2021-11-18/>.

<sup>29</sup> <https://www.adidas.com/us/metaverse>.

<sup>30</sup> See, e.g., *Roc-A-Fella Records, Inc. v. Dash*, 1:21-cv-05411-JPC (S.D.N.Y.), in which *Roc-A-Fella Records* initiated a copyright infringement lawsuit against its co-founder *Damon Dash* for improperly attempting to sell Jay-Z's "Reasonable Doubt" album as an NFT. *Roc-A-Fella* argued that (i) it owned all rights in and to the album, including the copyright, as a corporate asset and, therefore, (ii) *Dash*, a minority shareholder in the company, could not sell an asset he did not personally own. The court granted *Roc-A-Fella* a temporary restraining order, thereby barring the sale of the NFT. The litigation is ongoing.

liabilities, it is important for brands to conduct proper due diligence on these third parties.

### 1. IP Considerations

When choosing a partner for NFT minting and initial sales, advertisers should consider how such platforms will protect their brand's IP rights—not only in the underlying NFT Media but also in the brand's marks. The degree of protection desired will vary by brand and by instance. At a minimum, brands should ensure that any minting and initial sales platform has in place an End User License Agreement (EULA) or Terms of Service (TOS) that prevents misuse of trademarks, bars the creation of derivative works and prevents further commercial use. Additionally, brands should seek indemnification from any vendor partner for any third-party claims that may arise from a platform's infringement of others' IP.

### 2. Financial Regulatory Considerations

From a technical perspective, an NFT is fundamentally a blockchain-based digital asset or token, similar in many respects to a cryptocurrency. Accordingly, prior to minting and selling NFTs, brands should consider the potential application of financial regulations such as the securities laws, financial sanctions programs and anti-money laundering laws and regulations. At a minimum, advertisers should ensure that any third-party vendors (i) represent and warrant full compliance with applicable regulatory frameworks and (ii) indemnify them for claims that may arise from a failure to do so.

## Promoting Your NFTs

At the moment, NFT promotions are occurring primarily via online outlets such as social media platforms and email mailing lists.<sup>32</sup> Brands should consider the various advertising content restrictions that may apply for each outlet. Depending on whether the brand attempts to promote a paid advertisement versus generating an “organic” post via its own social media pages, different restrictions may apply. Importantly, if brands engage influencers to endorse and promote their NFTs, the Federal Trade Commission's Guides Concerning the Use of Endorsements and Testimonials in Advertising (FTC Endorsement Guides)<sup>33</sup> will apply.

<sup>32</sup> Traditional television media outlets have commercial clearance advertising guidelines in place that dictate whether certain ads may run on their channels. However, many of these guidelines have not yet been updated to include new technology such as cryptocurrency and NFTs.

<sup>33</sup> 16 CFR Part 255, available at <https://www.ftc.gov/sites/default/files/attachments/press-releases/ftc-publishes-final-guides-governing-endorsements-testimonials/091005revisedendorsementguides.pdf>.

### 1. Paid Advertising

Generally speaking, most social media platforms, including Meta, Twitter, Instagram and TikTok, restrict the types of content that may be promoted via paid advertising. As of the date of this publication, none summarily bars the advertising of NFTs, but most platform advertising policies contain caveats to such promotion.

For example, Twitter globally restricts the advertising of “[n]on-fungible tokens (NFTs) and related products,” *but* includes the suggestion that advertisers “interested in promoting NFTs or related products and services” contact Twitter.<sup>34</sup> TikTok prohibits the paid advertising of “virtual currencies” as well as “cryptocurrency trading platforms and advisory services,” but remains silent on NFTs specifically.<sup>35</sup> Google (whose policies control YouTube) prohibits advertisements for “initial coin offerings, DeFi trading protocols or otherwise promoting the purchase, sale or trade of cryptocurrencies or related products,” but, like TikTok, remains silent on NFTs.<sup>36</sup> On the other hand, Meta (whose policies control Facebook and Instagram) permits the advertising of NFTs provided that they are “[s]ervices and products based on blockchain technology that are not a virtual currency.”<sup>37</sup> The NFT market and the policies of social media platforms are constantly evolving. Before brands steer dollars toward paid advertising, they should consult applicable platform advertising guidelines to confirm that a particular NFT advertisement will be accepted.

### 2. Posts on Brands' Own Pages

While a platform's advertising guidelines govern the content of what a brand can include in paid advertising, it is a platform's community guidelines that govern the content of what a brand can post on its own social media pages.<sup>38</sup> Community guidelines set a common standard for all platform users to help ensure that speech on the platform can be expressed freely yet safely. They typically prohibit users from posting content that is violent, constitutes harassment or hateful conduct, discloses the private information of others, or promotes illegal activities.

<sup>34</sup> *Ads Help Center: Financial Products and Services*, Twitter, <https://business.twitter.com/en/help/ads-policies/ads-content-policies/financial-services.html> (last accessed April 25, 2022).

<sup>35</sup> *Branded Content*, TikTok, <https://support.tiktok.com/en/business-and-creator/creator-and-business-accounts/branded-content-policy> (last accessed April 25, 2022).

<sup>36</sup> *Advertising Policies Help*, Google, <https://support.google.com/adspolicy/answer/10688110?hl=en> (last accessed April 25, 2022).

<sup>37</sup> *Advertising Policies*, Meta, [https://www.facebook.com/policies/ads/restricted\\_content/cryptocurrency\\_products\\_and\\_services](https://www.facebook.com/policies/ads/restricted_content/cryptocurrency_products_and_services) (last accessed April 25, 2022).

<sup>38</sup> See, e.g., *Facebook Community Standards*, available at <https://transparency.fb.com/policies/community-standards/>; Twitter Rules, available at <https://help.twitter.com/en/rules-and-policies/twitter-rules>; Instagram Community Guidelines, available at <https://www.facebook.com/help/instagram/477434105621119>; and TikTok Community Guidelines, available at <https://www.tiktok.com/community-guidelines?lang=en>.

The content of a post promoting a sale or drop of a brand's NFT would likely not contravene current community guidelines. However, prior to the tweeting, 'gramming or TikToking of NFTs, advertisers should consult each platform's community guidelines and/or branded content policies, as these policies are also constantly evolving.

Additionally, advertisers should note that any post on a brand's own social media page—while it may not rise to the level of a paid ad on the platform—constitutes an advertisement under state and federal law, subject to regulatory scrutiny by both the FTC and state attorneys general under applicable consumer protection laws. Accordingly, any posts regarding an NFT cannot mislead consumers. Brands must be mindful to describe the assets, goods and/or services that are being offered in a clear and direct manner so as not to cause any confusion. For example, if a brand decides to offer a “limited edition” NFT, it must keep to this promise. Additionally, brands should avoid promoting an NFT as an investment or implying that it is an asset that may increase in value.

### 3. Influencer Posts

When a brand engages an influencer, or brand ambassador, to promote or endorse its NFT, the FTC Endorsement Guides will apply. These guides address the application of Section 5 of the FTC Act<sup>39</sup> to the use of endorsements and testimonials in advertising and establish certain protocols that must be followed in such promotions. It should be noted that while these guides do not themselves have the force of law, they provide a basis for voluntary compliance with the law by advertisers and endorsers and set forth the general principles by which the FTC will evaluate endorsements and testimonials.<sup>40</sup> Pursuant to the FTC Endorsement Guides, brands should employ the following best practices upon engaging influencers to promote NFTs:

#### a. Clearly and conspicuously disclose any material connection between an advertiser and influencer

This may come in the form of an included hashtag, e.g., #ad, #[Brand]Partner or #freeproduct. A “material connection” has been interpreted to include: (i) monetary compensation; (ii) the gifting of a free product; (iii) an employer/employee relationship; or (iv) a familiar relationship with an advertiser's employee (e.g., the wife of the influencer works for the advertised brand).

#### b. Limit claims made by influencers in social media posts

Claims should be limited to those that an advertiser itself could

support (with adequate substantiation) were the post to be made on the brand's own page or account. Any descriptions of the NFT sale, including accompanying goods, services or experiences, must be truthful. Even if truthful, the influencer should refrain from commenting that any NFT he or she owns has increased in value, as this can be misunderstood as an implied claim that other NFTs will do the same.

#### c. Expressly prohibit the use of certain claims

The following express or implied claims should be prohibited: (i) that an NFT presents an investment opportunity; or (ii) that an NFT's value may increase over time. Brands should inform influencers that such claims are impermissible.

#### d. Monitor posts to ensure compliance

Posts should be monitored for compliance with the FTC Endorsement Guides and any brand-specific advertising guidance. The influencer agreement terms should allow the brand to require an influencer to modify or remove any noncompliant post. Additionally, compensation can be tied to or contingent upon an influencer's compliance with these guides.

#### e. Understand platform influencer policies

The above rules are also addressed in many platforms' branded content policies, which govern how brand affiliates may post about products or services for which they receive something of value in exchange for the posts.<sup>41</sup>

#### f. Monitor influencers' social media accounts

Brands should monitor their influencers' social media accounts both during an active campaign as well as for a reasonable period thereafter. Not only should brands pay attention to the content that they pay for, but they also should pay attention to any out-of-scope brand mentions or posts made by the influencer that discuss a competitive brand. Active monitoring allows brands to ensure that posted content is compliant and provides time to take corrective action—such as requiring the influencer to edit or remove a post—if it is not.<sup>42</sup>

<sup>41</sup> See, e.g., *Facebook Branded Content Policies*, available at <https://www.facebook.com/business/help/221149188908254/>; *Instagram Branded Content Policies*, available at <https://help.instagram.com/616901995832907/>; *TikTok Branded Content Policy*, available at <https://support.tiktok.com/en/business-and-creator/creator-and-business-accounts/branded-content-policy>.

<sup>42</sup> Influencer posts have recently become an area of increased regulatory scrutiny. Last fall, the FTC sent over 700 companies a Notice of Penalty Offenses alerting them that they may be subject to civil penalties if they engage in unfair or deceptive conduct relating to the use of endorsements and testimonials. For more information on the FTC notices, see <https://www.ftc.gov/enforcement/penalty-offenses/endorsements>.

<sup>39</sup> 15 U.S.C. § 45.

<sup>40</sup> See 16 CFR Part 255.

### g. Take swift action to remove false or misleading statements

Brands can be held liable for false or misleading statements made by those who endorse or promote their products. The cryptocurrency market is no exception. Earlier this year, plaintiffs filed a class action in the Central District of California against EthereumMax, its executives and celebrity promoters for unfair and deceptive practices.<sup>43</sup> More specifically, the suit alleges that EthereumMax executives used celebrity endorsers Kim Kardashian, Floyd Mayweather and Paul Pierce to deceptively “hype” the market for the tokens and mislead consumers into investing in a “pump and dump” scheme. Although this suit concerns the endorsement of cryptocurrency tokens rather than NFTs, it may stand as a potential harbinger as to how the current laws may be applied to endorsements within the NFT marketplace and is likely indicative of what will be an active class action plaintiffs’ bar in this space.

## Reputational and Public Relations Considerations

A key consideration for advertisers—regardless of the product being promoted—is that the messaging surrounding the marketing aligns with a brand’s stated principles and, moreover, its consumers’ expectations. Admittedly, this is less a legal issue and more a public relations one. While an advertising campaign can follow all guidelines and be legally compliant, a brand may still end up facing public wrath for espousing views that run counter to their consumers’ beliefs or by engaging in partnerships and collaborations that violate the brand’s public ethos. Two arenas in which brands may encounter potential messaging issues related to the promotion of NFTs are sustainability and access.

### 1. Sustainability

Over the past decade, many brands, reacting to impending threats of climate change, have committed to incorporating more eco-friendly practices into their business models. However, such commitments to “sustainability” or “going green” can be at odds with the realities of creating and selling NFTs. The carbon footprint of minting an NFT is still being debated.<sup>44</sup> However, the environmental damage caused by the copious amounts of energy expended to mine the cryptocurrencies required to purchase NFTs is well known. Thus, there exists a tension between how consumers will perceive a brand’s claims of sustainability as juxtaposed with the brand’s adoption and promotion of NFTs.

<sup>43</sup> *Huegerich v. Gentile*, 22-cv-00163 (C.D. Cal., Jan. 7, 2022), later consolidated as *In re EthereumMax Investor Litigation*, 22-163 MWF (SKx).

<sup>44</sup> See Jiahui Qiu, *What Are NFTs, and What is Their Environmental Impact?*, Earth.org (April 20, 2021), <https://earth.org/nfts-environmental-impact/> (positing that because many steps within the NFT minting process do not have a known carbon footprint, calculating an NFT’s overall carbon footprint is difficult).

To help mitigate a potential public relations backlash, environmentally conscious brands may opt to partner with a blockchain that operates on the more energy-friendly “proof of stake” consensus mechanism versus the energy-consuming “proof of work” standard.<sup>45</sup> However, brands should also keep in mind that to the extent they tout the environmental benefits of a “green” blockchain in connection with the promotion of their NFTs, the FTC’s Guides for the Use of Environmental Marketing Claims (FTC Green Guides)<sup>46</sup> may apply. To the extent a company makes a general corporate commitment to reduce its carbon or fossil fuel energy use, consideration should be given to how venturing into the NFT marketplace may increase the company’s energy footprint.

Similar to the FTC Endorsement Guides, the FTC Green Guides do not have the force of law but provide guidance to marketers to help them avoid making deceptive or misleading environmental claims to consumers that may contravene Section 5 of the FTC Act. Generally, the FTC Green Guides suggest that an overall environmental benefit claim should be qualified and any specific benefit claim should be substantiated. This guidance would pertain to certain blockchains’ claims of being “carbon neutral” or providing a “carbon offset.”

### 2. Access

In the past few years, brand personalities have been at their highest level of scrutiny. Social consciousness has been at the forefront of brand identity. What a brand stands for can be as important as what a brand sells. Brands have increasingly embraced principles of inclusivity and accessibility and have raised their own awareness regarding the potential barriers to entry that exist in certain markets.

However, these principles may be in conflict with the potentially restrictive culture of cryptocurrency and NFTs. While brands see the marketing of NFTs as an opportunity to deepen their engagement with current and potential customers, some consumers may view a brand’s foray into the cryptocurrency and NFT market as potentially alienating, limiting access to certain customers based on socioeconomic status, technology and even gender. As with issues stemming from brands’ claims of sustainability, these matters are less in the legal realm and more in the public relations realm, but they are worth considering as brands expand into the digital universe.

<sup>45</sup> For a more detailed explanation on the differences between the two standards, see “What is ‘Proof of Work’ or ‘Proof of Stake,’” Coinbase, <https://www.coinbase.com/learn/crypto-basics/what-is-proof-of-work-or-proof-of-stake> (last accessed April 25, 2022).

<sup>46</sup> 16 CFR Part 260, available at [https://www.ftc.gov/sites/default/files/documents/federal\\_register\\_notices/guides-use-environmental-marketing-claims-green-guides/greenguidesfrn.pdf](https://www.ftc.gov/sites/default/files/documents/federal_register_notices/guides-use-environmental-marketing-claims-green-guides/greenguidesfrn.pdf).

## Consumer Protection: Proper Disclosures and Setting Expectations

### 1. Sweepstakes and Contests

Promotional giveaways involving NFTs—such as sweepstakes and contests—remain subject to the same rules and regulations governing traditional sweepstakes and contests. In short, they cannot constitute a lottery, which is comprised of the following three elements: (i) prize, (ii) chance and (iii) consideration. Except for permitted state-run lotteries, lotteries are otherwise illegal. Therefore, brands must structure any NFT sweepstakes or contest in a manner that eliminates any one of the three elements of a lottery. Specifically, a sweepstakes eliminates consideration by making entry completely free or by providing a free alternative method of entry (AMOE) if a paid entry option exists. A contest eliminates chance by selecting a winner based on objective criteria set forth in the official rules.

Sweepstakes and contests involving NFTs and the transfer of cryptocurrencies must also be mindful of unique elements inherent in the blockchain sphere. To avoid potential issues, best practice suggests that the official rules of any NFT-based sweepstakes or contest should:

- a. Require that only the winners (rather than all participants)** (i) have a digital wallet to accept the NFT prize and (ii) be subject to any digital wallet (or other) fees.
- b. Clearly and conspicuously disclose that the value of the NFT may fluctuate** due to market volatility by: (i) setting a fixed date for the prize valuation; (ii) disclaiming liability for any potential loss of value; and (iii) establishing a firm date by which tax liability will be established.
- c. Clearly and conspicuously disclose the winner's rights and limitations** in/to the NFT by: (i) informing winners what they can and cannot do with the underlying media file(s); (ii) informing winners that they will not be eligible to participate in any royalties that may stem from future sales of the NFT; and (iii) disclaiming liability for any future inability of the winner to access the underlying media files connected to the NFT resulting from (A) technological issues (including hacks) or (B) changes in legal or regulatory regimes.
- d. Additionally, brands will want to conduct due diligence** on any potential sweepstakes partner and require that any vendor: (i) indemnify and release the brand in connection with any issues stemming from the vendor's actions or inactions with respect to the promotion and administration of the sweepstakes; and (ii) include in any force majeure provision occurrences such as (A) cyberattacks and (B) hacks.

### 2. Potential Class Actions

A sweepstakes sponsor can be particularly susceptible to the risk of a class action if it fails to clearly and conspicuously disclose a free AMOE when the sweepstakes offers both a free and a paid method of entry. Recently, sweepstakes involving cryptocurrencies have become a target. In June 2021, a proposed class action was filed against cryptocurrency exchange Coinbase and its sweepstakes administrator, Marden-Kane Inc.<sup>47</sup> The suit alleged that Coinbase's email and web advertisements for its \$1.2 million Dogecoin sweepstakes were "specifically designed" to obscure the fact that consumers could enter the sweepstakes without needing to transact the advertised \$100 in Dogecoin on Coinbase. Plaintiffs alleged that by failing to clearly and conspicuously disclose this option, Coinbase intentionally deceived, misled and confused reasonable consumers into believing they needed to transact on the platform and pay Coinbase a commission for such transactions in order to enter the contest.

To avoid potential litigation when sponsoring a sweepstakes, best practice dictates that sweepstakes sponsors *clearly and conspicuously* disclose a free AMOE in all advertising when a sweepstakes includes both a paid and a free method of entry. Additionally, prior to launching any promotion, sweepstakes or contest, brands should consult with counsel to ensure compliance with local and federal laws.

### 3. Advertising to Children

Brands from Mattel to Marvel have embraced the NFT marketplace, offering digital wares ranging from Barbie dolls to comic books.<sup>48</sup> While these items may be designed to engender nostalgia in adult consumers, these kinds of digital offerings may also entice children under the age of 13. If a brand operates a website that targets or collects personal information from children under the age of 13, the Children's Online Privacy Protection Act (COPPA), which authorizes the FTC to make and enforce rules to protect children's online privacy, will apply.<sup>49</sup> Under COPPA, website operators that direct advertising to or knowingly collect information from children under the age of 13 must employ certain safeguards, including:

- a. Providing clear and conspicuous notice** of the information collected, including (i) how the operator uses such information and (ii) the operator's disclosure practices for such information.

<sup>47</sup> *Suski v. Coinbase Global, Inc.*, 3:21-cv-04539 (N.D. Cal., June 11, 2021).

<sup>48</sup> See *Northman*, *supra* note 18, and *Press Release*, *supra* note 13.

<sup>49</sup> 15 U.S.C. §§ 6501-6506. COPPA also provides states with a right of enforcement thereunder.

- b. Obtaining verifiable parental consent** for the collection, use and disclosure of personal information from children.
- c. Retaining collected information** for only as long as is needed to perform the disclosed task.
- d. Not disclosing the collected information** to third parties unless doing so is an integral part of the business.
- e. Providing parental access** to the collected information along with a method for deletion, if requested.
- f. Safely and securely handling** the collected information and treating it as confidential.

Importantly, COPPA also applies to any online service provider or website operator if the website is directed at a general audience—not children specifically—and the provider has actual knowledge that the website is incidentally collecting personal information (including name, address, email address or physical location) from children under the age of 13. Fines for violating COPPA can run as high as \$46,517 per violation.<sup>50</sup> As many NFT platforms and sites require the collection of personal information to enable a purchase or a sweepstakes entry, best practice dictates that brands not only comply with COPPA directly but also require COPPA compliance from any vendor website partner.

#### 4. Charitable Contributions

To test the waters of the NFT market, many brands launched initiatives in 2021 in which the proceeds from sales of branded NFTs raised funds for various charities. Taco Bell released a set of limited-edition taco-themed NFTs to raise money for its Taco Bell Foundation,<sup>51</sup> Charmin released its NFT(P) to raise funds for Direct Relief<sup>52</sup> and Coca-Cola released special-edition “loot box” NFTs to raise money for Special Olympics International,<sup>53</sup> to name a few. However, when a for-profit brand endeavors to raise funds on behalf

50 *Complying With COPPA: Frequently Asked Questions*, FTC (July 20, 2020), <https://www.ftc.gov/tips-advice/business-center/guidance/complying-coppa-frequently-asked-questions-0> (last accessed Feb. 11, 2022).

51 See <https://rarible.com/tacobell/sale>.

52 <https://news.pg.com/news-releases/news-details/2021/Charmin-Rolls-Out-First-Ever-NFTP/default.aspx>.

53 <https://www.coca-colacompany.com/news/coca-cola-to-offer-first-ever-nft-collectibles>.

of a nonprofit entity—whether via an NFT auction or sale—specific laws and regulations may apply.

##### a. State commercial co-venture laws

While they vary from state to state, these laws may impose additional contractual, registration and/or reporting requirements on the brand. At the very least, the best practice is for a brand to enter into an agreement with its chosen charity that sets forth: (i) the date(s) for the charitable campaign; (ii) how funds will be collected; (iii) the geographic scope of the campaign (e.g., retail sales within certain states, U.S.-only sales via the internet); (iv) the amount that will be donated to charity and how that amount will be calculated (e.g., 5 percent of proceeds); and (v) how the funds will be sent to the charity. Brands should always consult counsel to determine whether any additional requirements apply pursuant to state commercial co-venture laws.

##### b. State auction laws

If a brand decides to distribute its NFT via a charity auction, it must first conduct due diligence to ensure that the partner auction platform is properly registered in all applicable states pursuant to state auction laws. As with any brand promotion—but especially so with charitable ones—it is imperative that brands are transparent with their customers and clearly and conspicuously disclose in advertising (i) which entity will receive the raised funds and (ii) the portion of proceeds raised that will be donated to the charity.

#### Conclusion

While some may dismiss NFTs as a mere passing fad, the market's enthusiastic embrace of such technology suggests otherwise. However, with any expansion of the market, legal challenges and regulations are likely to follow and brands' innovative creations will likely be tested. To that end, the best practice is for marketing executives to consult legal counsel early and often to ensure that any and all campaigns are designed to limit liability and risk to the brand while simultaneously taking advantage of the unique opportunities offered by this nascent technology.

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