

Thorny issues about valuing NFTs

NFT

NON FUNGIBLE TOKENS

About this issue

This issue is based on recent work we have carried out in the blockchain markets, applying skills and experience we have gained from valuations of brands, intellectual property (IP), intangible assets and businesses over the last 30 years. It also reflects the views of others involved in the blockchain markets.

We have a background of working for professional consulting firms and businesses rich in intangible assets. Our specific skills and knowledge are in the fields of global business development, accountancy, finance, marketing, valuation and dispute resolution.



Introduction

The increasing popularity of, and problems surrounding, NFTs has prompted questions as to how or if they could be valued.

What are NFTs?

NFTs are forms of legal IP rights and obligations. They are digital assets that represent real objects like art, music, films and videos. These digital assets are collectible and are registered on a decentralized blockchain, mainly Ethereum. Each NFT consists of a digital file, such as an image. This file is paired with a smart contract, an encrypted unchangeable contract that sets out the rights of ownership and authenticity of the NFT.

As each NFT is unique, NFTs differ from blockchain cryptocurrencies such as Bitcoin, where all Bitcoins are the same as each other.

William Shatner



As an example, William Shatner (Captain Kirk in Star Trek) offered 120,000 NFTs featuring images from his life and career on the WAX blockchain, which sold out in minutes. The NFTs had rights to images including headshots and characters from his early acting days, other moments such as him hugging Leonard Nimoy (Spock), and bizarrely an X-ray of William Shatner's teeth. Owners of the NFTs could then:

- Sell them on a marketplace.
- Trade them with anyone.
- Trade with some confidence that every NFT is certified authentic, unique, and cannot be altered - although the legal rights can actually be uncertain.
- View an NFT's ownership and trading history.
- Display their collection on social media.
- Look at wish lists of others.



What is copyright?

When creating a work of art, the artist automatically gains the copyright to that work of art. Copyright literally means the right to copy, but has come to mean the body of exclusive rights granted by law to copyright owners for protection of their work. It generally lasts for 70 years after the death of the artist.

When a work of art is sold as an object it can be seen as a way of generating revenue from the associated copyright, and the copyright is not typically sold with the work of art. Another important way of generating revenue from such copyright is by licensing rights, such as to produce prints of the work of art. Copyright needs to be sold or licensed in a written contract.



Where NFTs can be bought

Some significant online platforms for buying and selling NFTs are OpenSea, Rarible, SuperRare, and Mintable. OpenSea is one of the largest, where users are able to trade a number of different digital collectibles, relating to art, music, domain names, trading cards and many more.



The costs of transacting NFTs can be significant compared with amounts being invested. In addition there are risks. For example, HERMÈS has sued over the collection of 100 MetaBirkins NFTs that include images of furry versions of its famous BIRKIN bag. HERMÈS has claimed that the MetaBirkins creator is a digital speculator who has been using the famous BIRKIN brand for use in creating, marketing, selling, and facilitating the exchange of NFTs. HERMÈS has also claimed these rip off the BIRKIN trade mark by adding the generic meta prefix, which refers to virtual worlds and economies where NFTs can be traded.

Changing technologies and trends



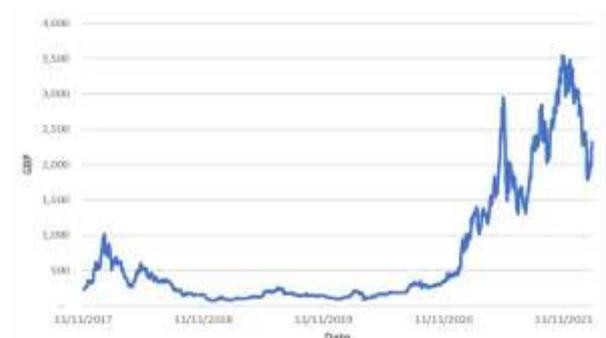
NFTs are a new way for artists to connect directly with fans and generate revenues. Predicting the revenues for doing so has the following issues:

- Future cash flows from the issue or sale of NFTs may encompass complex matters such as rights to new technologies, and further payments due to the artist on subsequent NFT sales.
- Comparable NFT prices will be hard to ascertain, analyse and compare.

The music industry is a good example of the impact of new technologies. Initial commercialisation of a song could have been primarily on 33 rpm vinyl records. However after that significant additional revenues could then have been generated through new technologies like CDs, streaming, and enhancement of existing channels such as concerts. An NFT might not cover use through future new technologies and trends, and in such circumstances the copyright to such revenues would reside with the artist, so long as it is within the copyright life. Predicting such new technologies and trends and their impact is necessarily fraught with difficulty.

The volatility of crypto currencies

NFTs are bought and sold using crypto currencies, principally Ethereum (which is the second largest cryptocurrency by market capitalization after Bitcoin). Prices of these crypto currencies have been highly volatile and difficult to understand, as shown by the chart below based on data from yahoo! finance on the Ethereum price to GBP:



Conclusion about assessing NFT values

There are a number of challenges when assessing values of NFTs, namely:

- Defining and understanding the legal and commercial rights associated with the NFTs.
- Predicting future cash flows relating to those rights, particularly if there is a disconnect between anticipated future cash flows and the reason for investment (such as building a collection).
- The high price volatility of crypto currencies used for buying and selling NFTs.
- Researching useful information on prices paid for comparable NFTs. As each NFT is unique close comparisons may not be possible, and transaction costs can be high, thus distorting any research and analysis.

Such challenges are also usually present to some extent when valuing other types of IP such as trade marks and patents. Although difficult and subjective, IP valuation techniques can be used to arrive at a more informed assessment of value, if that is required.

Valuation services offered by Intangible Business:

Our valuation services are based on professional and commercial knowledge and experience in accounting, marketing, investment banking, and research. We provide:

Analysis and opinions on:

- Business value.
- Brand, intangible asset and intellectual property value.
- Share value.
- Historic and forecast profits.
- Related revenues and costs.

Support in connection with:

- Business development, acquisitions, disposals, licensing and franchising.
- Financing and lending.
- For information, so that values of critical assets are measured and managed.
- Dispute resolution.
- Accounting for acquisitions and impairment.



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Thayne is a qualified accountant and marketer who has worked in consulting firms on valuation, dispute resolution and other special assignments since 1988. Thayne specialises in advising on all types of intangible asset valuation resolution projects on a range of issues across many different industries.

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