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# NFTs as Cryptoassets: The Next Dot-com Bubble?

## The Dot-com bubble and NFTs

The late 1990s to early 2000s were a time when the internet – still in its infancy – was akin to the wild-west; new, uncharted, and rapidly growing in usage and adoption. The accompanying excitement over this new technology fuelled a stock market bubble caused by untenable speculation on dot-com companies. The bubble finally burst in March of 2000, resulting in the NASDAQ *'falling by more than 75 percent between March 2000 and October 2002, thus wiping out more than $5 trillion [USD] in market value.'*[1] Given the similar rise and the prominence of Non-Fungible Tokens ('**NFTs**') in the headlines over the past year, one cannot help but draw parallels with the dot-com bubble. This poses the question of whether we are in middle of the next dot-com bubble and, should it burst, how much would be wiped off the value of the NFT market.

## What are NFTs and what is their purpose?

The word 'NFT' is an initialism which stands for 'Non-Fungible Token'. Broken down:

- **Non-Fungible means non-interchangeable**. Currency (e.g., USD) is an example of a fungible asset, whereas a piece of art is an example of a non-fungible asset.
- **Token means a unit of data stored on a blockchain** (a digital ledger) that can be sold and traded.

A blockchain in essence, is a database (or digital ledger) shared across a network of computers where records are added to a chain, and their authenticity is verified by participants in the network. This makes the chain difficult to alter or manipulate. It is on this chain of records where NFTs live.

As for what an NFT is, in simple terms it could be described as '*a certificate of authenticity for an object, real or virtual… [t]hat means that the chain of custody is marked in the file itself permanently, and it's practically impossible to swap in a fake*'[2]. If NFTs are unalterable digital certificates, they enable users – according to the Ethereum Foundation (the blockchain on which most NFTs are 'minted', or created, as at the time of writing) – *'to assign or claim ownership of any unique piece of digital data, trackable by using Ethereum's blockchain as a public ledger.'*[3] In theory, this means that a user could use an NFT to record ownership of any non-fungible asset, such as amongst others, digital and non-digital artwork, deeds to a car or a house, legal documents, invoices, by evidencing their ownership in a digital medium which is in principle invulnerable to tampering and or alteration with regard to its authenticity.

For example, an organiser selling tickets to an event mints NFTs evidencing ownership of the ticket that are non-transferrable, thus preventing them from later being resold by ticket scalpers at higher prices. As ownership of these tickets is evidenced by an NFT the tickets cannot be forged or altered as

[1] https://internationalbanker.com/history-of-financial-crises/the-dotcom-bubble-burst-2000/
[2] https://www.latimes.com/business/technology/story/2021-03-11/nft-explainer-crypto-trading-collectible
[3] https://ethereum.org/en/nft/

they are '*stored on the blockchain immutably*[4] *so that all parties can prove the ticket's authenticity*'[5] thus weeding out fake or forged tickets.

In practice, however, the use of NFTs today is mostly confined to evidencing ownership of digital content and artwork. Nevertheless, NFTs are revolutionising the digital art world by allowing artists to sell their work directly and receive the proceeds thus eliminating the need for intermediaries who would otherwise earn commission. Furthermore, some NFTs can be designed to automatically pay out guaranteed royalties to their original creator each time the NFT is resold. In turn, this provides autonomy to artists over the ownership of their work without handing over control to the platforms they use to publicise it.

**Are NFTs a Ponzi scheme and are they regulated?**

To a great extent, the present confinement of NFTs to the sale and purchase of digitally created content can be attributed to the absence or at least slow deployment of its other potential use cases. Consequently, this may help explain headlines proclaiming that scammers have made off with $2.7 million USD generated from the sale of pictures of cartoon apes[6] leading some sceptics and critics to dismiss NFTs entirely, and perhaps arbitrarily, as an elaborate Ponzi scheme. This negative perception is certainly not aided by the absence of a legal framework regulating the sale and purchase of NFTs, as well as the marketplaces which they are sold on. Hence, until the implementation of the latter the negativity publicity or public perception will probably persist.

**The regulatory landscape in Cyprus: The 'DLT' Bill of 2021**

Despite introducing a regulatory regime for services provided in relation to crypto-assets, Cyprus has not yet formally adopted any legislation providing legal substance to NFTs. Nonetheless, the proposed Distributed Ledger Technology ('DLT') Bill of 2021 (the "**DLT Bill**"), if enacted as drafted, may remedy some of the previously discussed issues.

The DLT Bill does not provide a formal definition for NFTs. Section 2 does however provide a definition for a token or cryptoasset as follows:

> '*a digital representation of value or rights which may be transferred and stored electronically using Distributed Ledger Technology or similar technology and is not:*
>
> *(i)* *issued or guaranteed by a central bank or public authority;*
>
> *(ii)* *a digital representation of an official currency of a country or electronic money, and thus does not have legal status of an official currency of a country or money;*
>
> *(iii)* *legal tender, whether or not denominated in legal tender.*'

Section 2 of the DLT Bill also categorises tokens into different types and provides the following definitions:

- Utility Tokens – a type of cryptoasset which is intended to provide digital access to a service, good or product and is accepted by the user of the token or participants in the ecosystem of that token;

[4] *Without them being altered or tampered with.*

[5] *https://www.leewayhertz.com/how-nft-ticketing-works/*

[6] *https://www.vice.com/en/article/y3dyem/investors-spent-millions-on-evolved-apes-nfts-then-they-got-scammed*

- Payment Tokens – a token, which is the digital representation of value and may be used as a means of payment or as consideration for the provision of goods or services, which is not issued by the authority of a central state authority, and which does not give rise to a claim on the issuer;
- Security Tokens – a token which constitutes a transferable security which is either created in a DLT platform or it is underlying and represented digitally and in such case the token may have all or some of the attributes of the underlying transferable security;

In addition to the above categories, section 2 of the DLT Bill also categorises tokens into the following types and provides the following definitions:

- Native Token – an asset or property that is issued directly one or more DLT systems or platforms, and is designated for ownership and electronic transmission;
- Non-Native Token – property that is meant to represent or is linked to conventional assets external to a DLT System, converted into digital format, or token representation of such, for ownership and electronic transmission. The non-native token can represent all or some of the attributes of the underlying asset or ownership.

It is clear from the above definitions that, in relation to the first type of categorisation, NFTs would fall under the broad definition of Token and constitute neither Payment nor Security Tokens but may fall under the definition of Utility Tokens. In relation  to the second type of categorisation, where NFTs claim ownership of a digital asset they might be deemed a Native Token and where they claim ownership of a unique physical asset, they might be deemed Non-native Tokens.

*Ownership*

Section 4(1) of the DLT Bill provides that tokens, '*irrespectively of whether they are digitally or non-digitally native* [i.e. native or non-native tokens] *are personal, movable property of the person they belong to*'. Importantly for NFTs certifying ownership of a physical asset, section 4(2) provides that '*in relation to* [Non-native Tokens] *the owner of the token has the same rights in the underlying asset as in the token*'. Section 5(1) provides that registration in the name of a specific person, natural or legal in a blockchain or other DLT system; or the possession of one or several private keys that are connected to a token '*constitute rebuttable presumptions of evidence of ownership of a token*'. Taken together sections 4 and 5 of the DLT Bill therefore provide a legal framework through which legal ownership of an asset (whether digital or physical) can be demonstrated through a blockchain network.

*Transfer*

Section 6 outlines the legal requirements which need to be met to execute a legally valid transfer of ownership of a token (whether fungible or non-fungible). Section 8 of the DLT Bill states that a record on a blockchain which was the product of error, deceit, or fraud is invalid. More importantly, it empowers Courts to *'order any person…to restitute the record or provide any other remedies for the restitution of the record or the damage caused.'* The latter provision should be beneficial for NFTs and DLTs by providing legal certainty and remedies should anything go wrong, which in the long-term could inspire both consumer and investor confidence in NFTs and DLTs by ensuring that they are not treated as unknown variables in the legal system.

## Conclusion

In the interim, until the enactment of the DLT Bill, judges will have to find a way of adjudicating any disputes concerning NFTs by 'creatively interpreting' existing rules and regulations to resolve them. Nevertheless, regardless of the present legal uncertainty and doubt over their practicality, NFTs need not be immediately written off as a speculative bubble provided that their development and deployment expands to include more practical or perhaps pragmatic use cases in more domains, and above all, that they manage to shake off the current negative perceptions surrounding their use. One way of doing so is ensuring that the law develops and matures in lockstep with NFTs; the proposed DLT Bill – at least in theory – may be a step in the right direction in achieving the aforementioned objective. Notwithstanding the present legal uncertainty in advance of the DLT Bill being formally enacted, our team is happy to assist with any IP, technology or cryptoasset/blockchain matters or disputes and can provide advice in relation to any NFT related matters.