Institute of Art and Law

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Julian Knight MP
Chair, Digital, Culture, Media and Sport Select Committee
House of Commons,
London,
SW1A 0AA

Dear Chair,

I was grateful for the opportunity to provide oral evidence to the Committee in relation to its enquiry into non-fungible tokens (NFTs) and the blockchain, in particular with regard to the arts sector.

In order to expand upon or clarify for the Committee a few of the matters discussed in the session where the opportunity for further elaboration did not arise, I am pleased to provide the following comments.

General/definitional matters

1. NFTs are essentially lines of computer code ('tokens') which link to or point to underlying assets, which can include both digital and physical works of art. They are unique and not interchangeable, one for another ('non-fungible').
2. Digital art: NFTs have proven particularly valuable to digital artists because of their quality of uniqueness and because they enable direct sales to buyers which can incorporate an automatic resale royalty through the operation of SMART contracts on a blockchain. Digital works sold through NFTs include (i) one-off creations (e.g. Beeple's famous work selling at over $69million in March 2021); (ii) artistic works sold by lesser known artists on a daily basis at much lower values; and (iii) collectibles (considered by some as 'art NFTs' and by others as a separate category) (e.g. the Bored Ape Yacht Club series).
3. Physical art: In relation to physical artworks, the primary role of NFTs is to provide an immutable, transparent and secure record of matters such as ownership and transaction history through blockchain technology.

Indication of the market/participation

4. Art NFTs remain a small proportion of the overall art market globally. The Art Basel and UBS Global Art Market Report 2023 estimates global art sales to have been worth $67.8 billion in 2022 (not including NFT sales on platforms outside the art market (p. 14)). Sales of art-related NFTs on such platforms stood at close to $1.5 billion, and of collectibles NFTs (treated separately in the report), at $11.8 billion (p. 37).
5. The number of buyers and sellers of art-related NFTs has risen very significantly in recent years. In 2019, there were more than 2,200 unique buyers and 1,800 unique sellers; in 2022 unique sellers stood

at more than 180,000 and buyers, 174,000 (note: this excludes buyers and sellers of collectibles, which would be a much higher figure; p. 35).

Risks for users/consumers

6. Copyright infringement is considered to be problematic in the NFT ecosystem. There are indeed plentiful reported examples suggesting a lack of understanding of or regard for copyright rules. However, one widely quoted statistic may have been a little misleading in this regard. This is the suggestion that 80% of NFTs on the world's largest NFT platform, OpenSea, are plagiarised, fake or scams. In fact, having stated that 80% of NFTs minted using a particular method (called 'lazy minting') violated its terms of service, the company later clarified the statement to explain that 80% of the items it *removed* for violations were minted using this method – a somewhat different proposition.
7. Consumer confusion was identified as a risk in the NFT market. It is worth noting that the Advertising Standards Authority has issued useful guidance on how crypto assets (including NFTs) should be advertised. Rulings have been issued against companies misleading customers by, for example, failing to illustrate the risk of NFT investment, failing to specify that an NFT did not have an assured significant value, and failing to clarify applicable fees (see the ruling on Turtle United NFT for an example).
8. An issue touched upon during the session related to the risk of NFT trading being used to launder the proceeds of crime. Whilst it is difficult to quantify this risk, blockchain analyst, Chainalysis, reported in its 2022 Crypto Crime Report that over $1 million worth of cryptocurrency was sent to NFT marketplaces by 'illicit addresses' in both of quarters three and four of 2021 (p. 35). The stringent anti-money laundering (AML) regime now applicable to art market participants in the UK trading above a specified value threshold (regulated by HMRC) and to the providers of certain crypto services (regulated by the FCA) do not clearly, and in all instances, apply to the NFT trading platforms. This could be a matter to keep under review with a view to including such stakeholders in the AML regime if proportionate and appropriate to do so.

Once again, I thank the Committee for the opportunity to contribute to this important work and would be delighted to assist further should this be helpful.

Yours sincerely,

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The Institute of Art and Law (IAL) is an educational organisation founded in 1995, engaged in teaching, research and publication in the area of art and cultural heritage law. It runs training courses for the museum sector in the UK and abroad and publishes academic and practical texts on many areas of law relating to cultural heritage and the arts. See more at www.ial.uk.com.