

Ownership Claims over Auction of “The First NFT” Previously Dismissed by a New York Court Now on Appeal

Blockchain and the Law on **September 28, 2023**

Way back (if we’re counting tech years) in 2014, artist Kevin McCoy (“McCoy”) created a [digital record](#) of his pulsating, octagon-shaped digital artwork [Quantum](#) on the Namecoin blockchain on May 2, 2014, thereby minting “the first NFT.” A lot has happened in the digital asset and NFT space since that day. Who could imagine that the mere creation of an original work of digital art whose provenance was immutably recorded on a blockchain (a novel act back then) would become a celebrated digital work that would garner almost \$1.5 million at auction seven years later? It’s likely that the artist McCoy also couldn’t foresee that such a sale would spur litigation in federal court over ownership rights surrounding the NFT he created.

Namecoin, an early blockchain and the first fork of the Bitcoin blockchain, is a system of “names” – unique combinations of numbers and letters – that can be claimed and traded by users. The Namecoin software is used to register names and attach associated values (data) to such names on the blockchain. It was created to provide a decentralized domain name system (DNS), which translates domain names people type into a browser into the numbers computers use to retrieve content on the internet. Namecoin allows users to register and manage domain names ending with the “.bit” TLD, which is not managed by a central authority (e.g., ICANN) like traditional domain extensions such as “.com.” Each domain name registered in Namecoin is associated with a unique token that represents certain rights and control over that particular domain. Ownership of the token grants the user control over the domain name and the ability to manage its settings, such as linking it to a specific IP address or other data. Specifically, as stated in Plaintiff’s [amended complaint](#), “In the case of Namecoin...each Namecoin record [can] store data within its blockchain records. This allows Namecoin records to be used like domain names, or to contain other values such as references to external images that allow them to act as NFTs.”

Most relevant to this litigation, ownership of every registered Namecoin name periodically expires, at which point any user may claim it and re-register the expired name if the original owner does not renew. McCoy's Namecoin name expired in January 2015 and remained unclaimed for the next six years. On May 28, 2021, McCoy minted a new NFT to record and preserve Quantum, but this time on the Ethereum blockchain ("Ethereum-Quantum"). McCoy stated that he "moved the original on-chain data from a burned Namecoin token into a modern, industry standard, ERC 721 token, while preserving all of the original on-chain information."

In May 2021, the auction house Sotheby's, Inc. ("Sotheby's") began marketing Quantum for an auction entitled [Natively Digital: A Curated NFT Sale](#) (with the listing describing Quantum (2014-21) as "Originally minted on May 3, 2014 on Namecoin blockchain, and preserved on a token minted on May 28, 2021 by the artist"). In the meantime, in April 2021, Plaintiff Free Holdings, Inc. ("Free Holdings" or "Plaintiff") had re-registered McCoy's original expired Namecoin token and thereafter asserted "title" to the Quantum NFT as it existed on Namecoin ("Namecoin-Quantum"), and then attempted to contact McCoy via Twitter to discuss its purported rights. Plaintiff's messages were allegedly ignored, and on August 23, 2021, Sotheby's sold McCoy's "re-minted" historic Quantum NFT for a reported sum of \$1,472,000. Litigation ensued.

In February 2022, Free Holdings sued McCoy and Sotheby's (collectively "Defendants") in New York district court, taking issue with the Defendants' statements that the Namecoin record associated with Quantum had been "burned" or "removed," and asserting unjust enrichment and related claims. Free Holdings also sought an order declaring that (i) Free Holdings is the rightful owner of the Namecoin-based Quantum; (ii) the Namecoin-Quantum has not been burned or otherwise removed from the Namecoin blockchain; and (iii) the statements issued by McCoy and Sotheby's in connection with their sale of the Ethereum-Quantum were false and misleading; and (iv) other damages and injunctive relief. In short, Free Holdings claimed that the Defendants presented an inaccurate narrative during the sale of the Ethereum-Quantum NFT and that Plaintiff lost an opportunity to profit.

According to the Plaintiff, “all subsequent activity associated with [McCoy’s originally minted Namecoin] is forever linked to that name on the Namecoin blockchain” and “all prior history associated with that name . . . cannot be deleted so long as the Namecoin blockchain continues to operate.” Plaintiff essentially claims it has the claim ticket to Quantum and thus obtained enforceable property rights in the Namecoin-Quantum NFT and any related future sales, including the sale of the Ethereum-Quantum NFT at Sotheby’s. Defendants countered that the statements and characterizations about the Namecoin-Quantum were not accurate, and that Free Holdings lacked any proprietary interest in the original Quantum NFT or the Ethereum-Quantum NFT or otherwise assert a concrete injury. Weighing the two sides: Plaintiff believed it has ownership rights in the Namecoin-Quantum through its registration of the expired Namecoin name, while Defendants alternatively argued that there are really two Namecoin NFTs – a “2014 NFT” originally registered by McCoy and a “2021 NFT” registered by Free Holdings – and that Plaintiff’s title to the re-registered “2021 NFT” was irrelevant to McCoy’s historic Namecoin NFT and its reminting on Ethereum.

Earlier this spring, the district court [dismissed](#) the complaint, both for lack of standing and for failure to state a claim. ([Free Holdings, Inc. v. McCoy](#), No. 22-881 (S.D.N.Y. Mar. 17, 2023)). In ruling against Plaintiff, the court rejected Plaintiff’s theory that its re-registering of McCoy’s expired Namecoin name somehow conferred a property interest in Quantum itself. The court pointed out that Free Holdings “nowhere alleges an interest in the NFT minted on Ethereum that McCoy and Sotheby’s sold” and that the Plaintiff even considered them two different NFTs. In the court’s view, Free Holdings adequately alleged a proprietary interest in the Namecoin-Quantum NFT for standing purposes, but it failed to advance any facts to support its claim to ownership of Quantum merely based on its re-registration of the Namecoin-Quantum NFT.

“[B]ecause no facts are alleged to suggest that Free Holdings had any claim to a share in the sale in the first place, there is no basis to support an inference that an injury occurred.”

The court further found that Free Holdings failed to allege any actual or imminent harm to the value of the Namecoin-Quantum, thus dooming any claims related to defendants’ statements or actions that purportedly devalued the Namecoin NFT.

Overall, as to the other unfair competition-related claims, the court stated:

“Free Holdings has demonstrated nothing more than an attempt to exploit open questions of ownership in the still-developing NFT field to lay claim to the profits of a legitimate artist and creator.”

Further, the court rejected any allegations that Defendants made any false statements surrounding Quantum during the sale of the NFT – the Defendants’ description of the Ethereum-Quantum explained that the work was “[o]riginally minted on May 3, 2014 on Namecoin blockchain, and preserved on a token minted on May 28, 2021 by the artist,” and that the artist “moved the original on-chain data from a burned Namecoin token into a modern, industry standard, ERC 721 token” was not substantially false, according to the court, and simply one interpretation of what happened when McCoy’s original Namecoin registration expired and was moved to Ethereum.

This dispute highlights a few interesting issues inherent with NFTs. First, in a [prior post from December 2022 following the Ethereum Merge](#), we asked: Would the value of the NFT be affected if two identical copies exist on two different blockchains? And in a [follow-up post on Ordinals on the Bitcoin blockchain](#), we asked: How does a copy of an NFT on completely different chain (Bitcoin, not Ethereum), affect value and licenses? Does the original Ethereum NFT holder hold one set of rights and the holder of the copycat on Ordinals possess any rights that may be in conflict with the original NFT holder’s rights? Our prior post noted that [there will be variability in how current NFT marketplaces handle these types of issues](#).

To be sure, the quirks of Namecoin – that is, the fact that names periodically expire unless renewed and the existence of a lack of consensus about what it means, from an ownership perspective, for someone to re-register an expired name – may not be present in other NFT-related disputes where the minter of an NFT would presumably hold rights to the token unless it was otherwise sold, transferred or licensed to a third party. Still, it seems from the Namecoin dispute we’ve seen firsthand how two NFTs could exist at the same time with only one of them possessing value in the marketplace. It appears in the instant case that the buyer at auction recognized that even though First Holdings held a claim ticket of sorts to some iteration of the Namecoin-Quantum NFT, it wasn’t holding the one that mattered. This is why Sotheby’s was able to broker the \$1.472 million sale of the Ethereum-Quantum NFT evoking the original, celebrated 2014 NFT, propelled by the cachet of acquiring what could be a relic from the dawn of NFTs (following the sale, the buyer [tweeted](#): “So happy to own the first ever NFT, Quantum, from @mccoyspace. A piece of history. Let’s see how we can continue its story.”).

Following the district court decision, the Plaintiff filed an appeal of the order dismissing the case to the Second Circuit. This summer, the parties advanced their arguments: the Plaintiff-Appellant filed its [brief](#) in July 2023, the Appellee-Defendants filed [opposition](#) on August 29, 2023, and the Plaintiff-Appellant filed its reply brief on September 12, 2023.

- Among other things, Plaintiff argues that the lower court erred when it resolved an alleged factual dispute that Free Holdings’ re-registration of the expired Namecoin name did not confer a cognizable property interest in Quantum itself, thereby tainting the court’s analysis of standing. (“If Free Holdings does have a ‘property interest in Quantum itself,’ as it has properly pleaded and thus the Court must assume at the pleading stage, Free Holdings cannot be the illegitimate intermeddler portrayed by the District Court, and can proceed to the merits on its claim....”).
- In opposition, Defendants states that the district court correctly found that the Plaintiff-Appellant lacked standing (“The District Court correctly found that Appellant sought nothing more than to take advantage of the nascency of the NFT market to manufacture baseless and legally flawed claims” [...] and that “the Court endorsed McCoy’s point that Appellant ‘never alleges that it can or could control’ the 2014 Namecoin NFT”).

Just like the Quantum NFT artwork that is constantly in motion, this case continues to revolve.

[View original.](#)