

The Metaverse and International Arbitration – How to Anticipate and Resolve Web 3.0 Disputes

By Juliette Asso and Laura Azaria

It's boom time for the metaverse – over the past few months, tech giants, clothing brands and anonymous individuals have invested hundreds of millions of US dollars in the metaverse. Virtual real estate prices have skyrocketed. And this is only the beginning of the metaverse era. But how can legal concepts created for the physical world protect investors in this new virtual environment? The metaverse will undoubtedly give rise to new and complex legal issues, and investors should take all preventive measures to safeguard their rights. International arbitration, as a flexible alternative to national judicial systems, will play a key role to resolve digital disputes.

As Facebook CEO Mark Zuckerberg would say, the metaverse is “*the next generation of the internet*”. It is basically a virtual environment you can enter – instead of just observing it on a screen – where you can (or soon will be able to) work, play, socialize, shop designer brands, buy virtual land and build skyscrapers, and a lot more. What makes the metaverse special nowadays, as compared to interactive videogame universes or social media, is the ability to buy, own and resell digital assets, a feature that has been enabled by the development of the blockchain technology. Also, the metaverse allows people to escape the individual, geographic and social limitations that bind them. Although it still is at an early developmental stage, the global metaverse market is expected to reach USD 758 billion by 2026.¹ As with any groundbreaking technological development, the metaverse will give rise to complex legal issues.

Disputes relating to NFTs

Legal disputes are already surfacing in the courts, particularly when it comes to the right to create and sell non-fungible tokens (“NFTs”), which are digital assets stored on a blockchain that represent real-world objects

¹ <https://www.strategyr.com/market-report-metaverse-forecasts-global-industry-analysts-inc.asp>

like art, music, or videos. In January 2022, the French luxury group Hermès filed a trademark lawsuit against digital artist Mason Rothschild for creating and selling 100 MetaBirkin NFTs depicting the company's iconic Birkin bag. While each MetaBirkin NFT was initially sold for a rather modest 0.1 ETH (the Ethereum blockchain's cryptocurrency), prices have skyrocketed since. According to Mason Rothschild, comparing his use of the Birkin to Andy Warhol's famed use of the Campbell's soup cans in the early 1960s, it is merely selling art. The latest high-profile intellectual property battle related to the metaverse involves Nike, which in early February 2022 sued reseller StockX, claiming that it was selling NFTs that display Nike's trademarks without authorization.

Given the current uncertainties surrounding intellectual property rights in the emerging NFT and metaverse industry, brand owners should take preventive measures before any disputes arise. This is, for instance, what led many brands, such as Nike, to file new trademark applications for use in the virtual world.

Several lawsuits will also arise in relation to contracts entered into before the metaverse era. For all intellectual property contracts drafted before the metaverse was even contemplated, a major source of contention will be to determine who owns the said rights in the metaverse and whether they include the right to mint (create) a corresponding NFT. This issue was at the core of the lawsuit filed by Miramax, the production company, against director Quentin Tarantino, following the announcement to auction off NFTs of seven exclusive scenes from his handwritten Pulp Fiction script. Miramax argues that Tarantino's NFT project violates their contract – although the contract was concluded long before the invention of NFTs. Going forward, it will be critical to draft contracts specifying who owns the intellectual property rights in relation to NFTs and the metaverse.

The Hermès, Nike or Miramax-Tarantino lawsuits are far from being the only type of Web 3.0 disputes. There are also going to be numerous claims by users against metaverse platforms² or among metaverse users. Although there will certainly be new types of disputes, the metaverse world will also

² There are currently not one but dozens of different metaverse platforms, the biggest being The Sandbox, Decentraland, Cryptovoxels and Somnium Space. Combined, they constitute "the" metaverse.

give rise to disputes of the same nature we encounter today in the physical world. This is because the communication means are changing between people, but the reasons for conflicts remain the same.

Disputes against metaverse platforms

The most obvious and predictable type of disputes that will arise between users and metaverse platforms will concern the violation of users' personal data, as it is virtually impossible for metaverse platforms to guarantee the absence of hacking attacks indefinitely.

A growing number of disputes relating to virtual real estate in the metaverse are also likely. The virtual real estate market is booming. Prices have recently reached unprecedented levels, with a total volume of USD 500 million last year (including a single transaction of USD 2.43 million in Decentraland) and are expected to double in 2022.³ What increases the value of a specific plot of land is not only its location but also its scarcity, since most metaverses guarantee a limited number of available plots. But what if the value of your waterfront parcel in a very trendy Saint-Tropez-like village suddenly falls, as the metaverse platform decides to build an airport instead of the virtual sea in front of your house, or to remove the sea altogether? Would you have a legal claim? Should you (and can you) ask for more guarantees than those provided by default, when buying your plot of land? And what if, despite its current commitment, a metaverse platform unilaterally decides one day to increase the number of plots? The value of your real estate investment would undoubtedly decrease, but would you have a claim against the platform for breach of its commitment to limit virtual land? Lastly, what if a metaverse platform goes bankrupt altogether or shuts down its servers? What claim would you have against it? Which bankruptcy law would be applicable?

There may also be disputes concerning the interference of metaverse platforms on users' personal investments in the metaverse, where they are allowed to offer services to other users or to create digital assets and sell them to other users. But what if, after having invested a fortune in building a state-of-the-art virtual flagship store, exhibition center, concert hall or

³ <https://www.cnn.com/2022/02/01/metaverse-real-estate-sales-top-500-million-metametric-solutions-says.html>.

gaming experience, the metaverse platform unilaterally decides to shut it down, or even delete your account altogether, because it finds your activity to be against its policy (which always contains a degree of subjectivity)?

In light of the above, before investing in the metaverse, players should assess the guarantees offered by the metaverse platforms, and their rights in case of violation, which vary from one platform to the other. This includes carefully reading the terms of use, with a particular focus on the following topics:

- The type of activities that are prohibited;
- The scope of the metaverse platform's limitation of liability: some platforms (The Sandbox and Decentraland) limit their liability for example in case of a bug or virus in the metaverse software, which may impact the services a user is offering or its digital assets;
- The existence of an overall limitation of liability cap (*e.g.* USD 100 for The Sandbox and Decentraland);
- The governing law and its impact on the users' rights and obligations. Currently, Decentraland provides for the laws of Panama, The Sandbox for the laws of Hong Kong and Cryptovoxel for the laws of New Zealand;
- The dispute resolution method: currently, arbitration under the ICC rules for Decentraland and jurisdiction of the courts of Hong Kong for The Sandbox.

Disputes amongst metaverse users

As for disputes amongst metaverse users, in addition to the trademark and ambush marketing disputes or the crime and tort disputes that will inevitably be replicated from the physical world (such as theft of digital assets, sexual harassment practiced by one avatar on another, housing disputes between neighbors, *etc.*), a large part of disputes will arise from transactions between users.

In the metaverse, users can:

- (i) offer services to other users (*e.g.* gaming experience, concert, real estate agency services, coaching);

- (ii) create digital assets (e.g. wearable, accessories, art) and sell them to other users; and
- (iii) rent or resell parcels of virtual land to other users.

But what terms and conditions apply to these transactions? Technically, these transactions are completed through smart contracts, which automatically transfer (permanently or temporarily) the ownership of the digital asset (*i.e.* the virtual land, the virtual object, or the virtual voucher giving access to the virtual service) from one user to another upon reception of crypto-payment. However, these smart contracts are currently limited to monetary obligations and term limitations; they do not allow users to provide for more complex rights and obligations to govern these transactions. In some specific circumstances, it might therefore be advisable to also enter into a “classic” contract specifying in particular the real identity of the avatars and the applicable law and dispute resolution mechanism chosen by them. The applicable law would address all the issues that could not be anticipated upon coding of the smart contract, or drafting the “classic” contract.

Alternatively, metaverse platforms could also start providing fair, transparent and impartial dispute resolution mechanisms for disputes between users. They could, for instance, allow disputes amongst users to be decided by a third-party user through a decentralized justice system, similar to the one used by eBay in the early 2000s. They could also provide for automatic enforcement of these decisions, which would be particularly important given the avatars’ anonymity. The successful performance of a specific metaverse will undoubtedly depend on its ability to address these dispute resolution issues.

Conclusion

The dispute resolution framework will have to be reinvented to account for the technological settings of the new environment we are moving into. Our legal system is based on geography because it is the world we currently live in. But in the metaverse – where anonymous avatars from all around the world are interacting and transacting with each other, time, location and identity are fluid perceptions. The legal concepts of habitual residence, place of business of the parties or real estate property location, which are

traditionally at the core of private international law rules, become meaningless in this context.

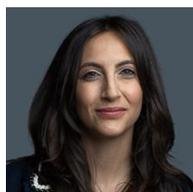
Therefore, before investing on the metaverse market, any investor would be well advised to carefully check the applicable terms of use, if any, and in certain circumstances, enter into a contract better suited to the particular needs of the transaction.

In case of disputes, contracts should allow for arbitration (after a potential mandatory mediation) rather than court litigation. These alternative dispute resolution mechanisms offer valuable advantages for digital transactions, provided they adapt to meet the challenges of technology and time-sensitivity:⁴ ability to agree in advance on the applicable law or the language of the proceedings, flexibility of the process, arbitrators' expertise in the technologies at hand, ease of enforcement of arbitral awards under the New York Convention, *etc.*

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⁴ The ICC has launched a report to assist tribunals and parties in leveraging technology for fair, effective, and efficient international arbitration proceedings (<https://iccwbo.org/media-wall/news-speeches/icc-launches-new-report-reflecting-how-tech-is-changing-the-face-of-arbitration/>).