

that CONTU felt was adequate 12 years later.

As a long-time lawyer in the art law field, I'm familiar with legal concepts dating back hundreds of years being applied to new media created using new technologies. But is it satisfying to take the literal words of the U.S. Copyright Act, a statute enacted in 1909, or even the conclusions of regulators acting in 1966 or 1978, and carry them through to situations which, we can agree, would have been unthinkable back then, such as an algorithm producing "A Recent Entrance to Paradise" without any human input whatsoever. And does it serve the interests of copyright law for *Paradise* to carry no copyright protection at all?

Thaler argued that, as a matter of policy, it made more sense to allow people in his position to register copyright in works created by their computers than to claim –falsely – that they themselves were the authors, and obtain registrations that way. It's important to remember that had Thaler asserted that he participated in the creative process *in any way*, the Copyright Office would have registered the work. They said as much in reciting the authorities upon which they were *denying* him registration. Our laws should not be limited by prior eras' concepts of who can or cannot create art. Whether those limits are enforced by refusing Naruto his day in court, or by prohibiting Thaler from protecting his computer-generated works from

infringement by others, they still are limits that should be reexamined with today's perspectives and not those of the past. ♦

<sup>1</sup> Principal, Law Offices of Armen R. Vartian. Vartian is Editor of this Newsletter, but the views in this article are his alone and not necessarily those of the ABA Art & Cultural Heritage Law Committee.

<sup>2</sup> U.S. Copyright Review Board correspondence ID-1-3ZPC6C3; SR #1-71003877071 (Feb. 14, 2022).

<sup>3</sup> *Naruto v. Slater*, 888 F.3d 418 (9<sup>th</sup> Cir. 2018).

## Treasury Study re Money Laundering in the Art Market: Some Risks— But No Immediate Government Action Required

By: Birgit Kurtz<sup>1</sup>

In February 2022, the U.S. Treasury Department issued its long-awaited Study on money laundering in the art market.<sup>2</sup> The findings are a mixed bag. While some sections of the art market were determined to be vulnerable to money laundering, others are deemed to have less exposure. The Study's recommendations for regulatory action vary accordingly.

### Background<sup>3</sup>

United States anti-money laundering (AML) laws, including the Bank Secrecy Act (BSA) and related regulations, are designed to help identify the source, volume and movement of currency in order to assist U.S. Government agencies in detecting and preventing money laundering; some of the laws are also designed to counter the financing of terrorists (CFT). These laws cover banks and certain enumerated nonbank financial institutions, including casinos, securities and commodities firms, insurance companies, and dealers in precious metals, stones, or jewels. Covered entities are required to *proactively* assist in the battle against money laundering.

In early 2021, Congress amended the BSA by adding a new type of "nonbank financial institution" to the list of covered entities:

a person engaged in the *trade of antiquities*, including an advisor, consultant, or any other person who engages as a business in the solicitation or the sale of antiquities.

Final regulations for these newly covered entities will likely be issued sometime in 2022.

### Art Market Study

To determine whether the *art trade* should also be covered by the BSA, Congress commissioned a Study obligating the Treasury Secretary to research money laundering and terrorist

financing in the art market. On February 4, 2022, the Treasury Department released the results.

The Study concluded that, compared to other industries with higher money laundering risk, "the art market should not be an immediate focus for the imposition of comprehensive AML/CFT requirements." Based on some of its inherent characteristics (*e.g.*, lack of transparency, easy transfer of high-value items, inconsistent due diligence practices), the art market is, in fact, vulnerable to abuse by criminals looking to launder illicit financial gains. But those risks are not equally distributed across the U.S. art market.

### Different Risks

The Study divided the art market into segments and assigned different risk levels:

**Auction Houses:** Because of the auction business model and related financial incentives, auction houses are "potentially vulnerable to abuse by illicit actors for ML purposes," even though most of them have AML/CFT compliance programs – albeit voluntary ones.

**Galleries:** Because they know most of their customers, are interested in maintaining a trustworthy reputation, and are not interested in selling entire collections to just one buyer, galleries "would likely not be the preferred venue for illicit actors to launder large volumes of funds."

**Art Fair Organizers:** Because they make money by renting space to galleries, not by selling artworks, organizers of art fairs are "less vulnerable to exploitation by launderers."

**Online Marketplaces** (*e.g.*, online viewing rooms – OVRs, eBay): The difficulty to verify the identities of buyers and sellers makes online marketplaces vulnerable to money laundering.

**Museums, Universities and other Nonprofits:** Museums are vulnerable to tax evasion and ML schemes when they acquire artworks; in the rare cases when they sell works, they are vulnerable to ML risks because they are unlikely to have necessary due diligence policies in place. For the same reasons, universities and other nonprofits are vulnerable to ML, but less so than museums because they do not generally rely on artwork donations and other art deals.

**Third-Party Intermediaries** (*e.g.*, interior designers, art advisors): When intermediaries are involved in art purchases without disclosing their clients' identities, such transactions and the involved parties are vulnerable to ML.

**Art Finance** (*e.g.*, art lending firms, auction houses with lending programs): Organizations involved in art finance face ML risks to the extent they do not follow robust AML/CFT compliance programs, especially "know your customer" (KYC) due diligence procedures.

**Banks:** Because they are covered by strict AML/CFT regulations, banks are "less susceptible to ML involving high-value art than other art market participants."

**Free-Trade Zones and Art Storage Facilities:** Because title to artworks held in storage areas can be easily transferred between different persons or entities, there are ML vulnerabilities in domestic storage facilities. International facilities (*i.e.*, free trade zones), however, are deemed less vulnerable because of existing regulations, voluntary practices and information collection by customs authorities. But because there is a

risk of collusion between different players, the Study suggests vigilance by customs officials.

Emerging Digital Art (e.g., non-fungible tokens – NFTs): The Study reasoned that “NFTs can be used to conduct self-laundering, where criminals may purchase an NFT with illicit funds and proceed to transact with themselves to create records of sales on the blockchain.” It also cautioned that transaction structures used for digital art “can create perverse incentives and ML vulnerabilities.” The Study, therefore, deemed emerging digital art vulnerable to ML risks – at least in part because art market participants who may otherwise have solid knowledge of the traditional art market, may lack “the technical understanding of distributed ledger technology required to practice effective customer identification and verification in this space.”

**Recommendations**

Based on the perceived risk of money laundering in the different sectors, the Study’s recommendations included the following actions:

- Companies that provide art financing

services should be covered by AML/CFT regulations.

- If other art market participants were to be regulated, entities with annual sales of less than \$500,000 or \$1 million should be exempted.
- Small and medium-sized art businesses should be assisted through the creation of an “information sharing mechanism” that would facilitate customer due diligence efforts without disproportionately increasing compliance burdens.
- International harmonization of art market regulations (e.g., with the EU and UK) should be considered.

**Conclusion**

As the art world’s “historic resistance” to KYC due diligence efforts has weakened, and trust in

“firewalls” (strict separation between compliance and sales departments within organizations) has increased, *voluntary AML/CFT compliance programs have already done much of the necessary work* to protect large parts of the art market from financial crimes. Because the Study has identified only a few areas within the art market that appear to be highly vulnerable to money laundering, it follows that any regula-

tions issued in the future should be narrow and targeted. If and when such regulations come into effect is, however, anyone’s guess. ♦

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<sup>2</sup> [https://home.treasury.gov/system/files/136/Treasury\\_Study\\_WoA.pdf](https://home.treasury.gov/system/files/136/Treasury_Study_WoA.pdf)

<sup>3</sup> See also Birgit Kurtz, “Recent U.S. Regulatory Developments Relevant to the Art Market,” ABA ILS Art & Cultural Heritage Law Committee Newsletter, at 3-4 (Spring 2021)

**New Lawsuit against Sotheby’s Raises Questions as to What Makes an NFT an NFT**

By: Laura Tiemstra<sup>1</sup>

One of the benefits of NFTs is digital security, i.e., that an NFT is unique and cannot be a forgery. In the art world, that security adds significant value. But more and more lawsuits are illuminating the many ways that NFTs, despite containing original blockchain, may not be lawfully made or sold.

The ease and access of high resolution photographs allows anyone to make an NFT of an image created by someone else; you may buy the NFT and know that it is the original NFT, but the creator of the underlying image may assert ownership rights against your NFT on the grounds of copyright infringement.

And what aspects of an NFT make it that specific NFT and not another? This is the subject of a lawsuit currently pending against Sotheby’s and artist Kevin McCoy in the federal district court for the Southern District of New York.<sup>2</sup>

NFTs are digital content (in this instance a GIF, but they also can be still images, videos, etc.) that are linked to unique blockchain, typically making authentication easy to establish. But arguably not in this case.

McCoy created what is allegedly the world’s first known NFT, titled “Quantum”, in 2014 on the blockchain Namecoin. NFTs minted on Namecoin contain both the unique blockchain

and metadata (in this case a GIF), similar to a domain name, which can then hold the website content. Also like a domain name, NFTs on Namecoin must be regularly renewed; failure to renew results in expiration of the ownership of that NFT, which then becomes available for purchase by third parties.

In March 2021, Axios published an article featuring McCoy and his “Quantum” NFT, and indicated that the NFT was about to be up for sale. Axios speculated that the “World’s first NFT” could sell for as much as \$7 million.

Unfortunately, McCoy had allowed his ownership of the “Quantum” NFT to lapse back in



2015. A few days after the Axios article was published, Free Holdings, Inc. purchased the NFT. Free Holdings allegedly immediately began attempting to engage McCoy in a discussion to have McCoy participate in selling the