October 12, 2024

**VIA ESMA WEBSITE**

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**Re: European Supervisory Authorities; Consultation Response (Consultation on Guidelines on templates for explanations and opinions, and the standardised test for the classification of crypto-assets under MiCAR: Consultation on Guidelines on templates for explanations and opinions, and the standardised test for the classification of crypto-assets under MiCAR form)**

Dear Chairpersons Campa, Hielkema, and Ross:

Andreessen Horowitz (“a16z”) appreciates the opportunity to respond to the European Supervisory Authorities’ (“ESAs”) consultation paper on their standardised test for the classification of crypto-assets under MiCAR[[1]](#footnote-0), published on July 12, 2024 (the “Consultation Paper”).[[2]](#footnote-1) We welcome opportunities to meet with ESA staff, answer any questions that the authorities may have, and discuss our comments below in more detail.

A16z is a venture capital firm that invests in seed, venture, and late-stage technology companies, focused on AI apps and infrastructure, American Dynamism, bio/healthcare, consumer, crypto, enterprise, games and fintech . A16z currently has more than $43 billion in committed capital under management across multiple funds, with more than $7.6 billion in crypto funds. In crypto, we primarily invest in companies using blockchain technology to develop protocols that people will be able to build upon to launch Internet businesses. Our funds typically have a 10-year time horizon, as we take a long-term view of our investments, and we do not speculate in short-term crypto-asset price fluctuations.

1. **Introduction**

We support the overarching objectives of MiCAR to create a single market for offering crypto-assets and the provision of related services across the EU. We therefore welcome the ESAs’ efforts to develop a common rulebook to foster convergence in approaches to supervision. Once finalised, the ESAs’ guidelines have the potential to reduce misunderstandings and misinterpretations of policy and regulatory intent, which will significantly strengthen the crypto industry in the EU. However, in order to achieve this result, we urge the ESAs’ to reconsider certain positions in the Consultation Paper. Our comments and observations are summarised below.

* Given that non-fungible tokens (NFTs) are outscoped from MiCAR, the ESAs should reconsider their inclusion in the Consultation Paper. The EU’s co-legislative bodies agreed in the MiCAR trilogues to exclude NFTs from MiCAR because many NFTs, such as digital art NFTs and music NFTs, are not primarily financial instruments. Thus, any attempt to introduce criteria that could result in the inclusion of broad categories of NFTs in the scope of MiCAR may contravene the regulation and create confusion in the marketplace.
* Several specific conditions and criteria pertaining to NFTs, including those contained in the referenced “Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments”[[3]](#footnote-2) and recital 11 of MiCAR should be reconsidered.
* The maximum consideration threshold for inclusion in MiCAR’s small and medium-sized enterprises (“SMEs”) and start-ups exemption should be raised from EUR 1 000 000 over a period of 12 months to EUR 5 000 000 over 12 months. For small businesses, the need to undergo the standardised test and in some cases comply with the full breadth of MiCAR’s relevant requirements may otherwise be extremely burdensome and stymie its goal of supporting innovation in the market for crypto-assets.

**Q4: Do respondents have any comments on the standardised test?**

As above mentioned, we welcome the ESAs’ efforts to develop a standardised test for the classification of crypto-assets to foster convergence in approaches to supervision and a predictable regulatory environment. We also appreciate the ESAs’ recognition that the regulatory classification of crypto-assets necessitates case-by-case evaluation. However, we are concerned that the ESAs’ standardised test contravenes the intent of MiCAR in several ways that could undermine the regulation’s objectives. Our concerns centre on the Consultation Paper’s treatment of NFTs as well as its implications for startups.

1. **Non-fungible tokens**

We appreciate the ESAs’ recognition that MiCAR does not apply to crypto-assets that are unique and non-fungible with other crypto-assets,[[4]](#footnote-3) which we note aligns with the intent of the regulation.[[5]](#footnote-4) The EU’s co-legislative bodies agreed in the MiCAR trilogues to exclude NFTs from MiCAR because many NFTs, such as digital art NFTs and music NFTs, are not primarily financial instruments. This exclusion is clearly stated in MiCAR, whereas ideas referenced in the Consultation Paper such as an “indicator of [...] fungibility” only appear in a suggestive form in the regulation’s recitals. Thus, any attempt to introduce criteria and indicators that could result in the inclusion of broad categories of NFTs in the scope of MiCAR may contravene the letter and the spirit of the regulation, which we believe requires a more focused, principles-based analysis of the NFTs in question.

As such, we are concerned that the ESAs’ recommendations relating to assessing non-fungibility of crypto-assets may be premature at this time. In particular, the Consultation Paper states: “In assessing if the crypto-asset is unique and not fungible, competent authorities and other persons to whom these Guidelines apply should have regard to Article 2(3) and recital (11) of Regulation (EU) 2023/1114 as well as the Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments.”[[6]](#footnote-5) These references — to both the European Securities and Markets Authority’s (“ESMA”) consultation paper on its draft guidelines on the qualification of crypto-assets as financial instruments for MiCAR (“Draft Guidelines”) and recital 11 of MiCAR — introduce indicators of fungibility that could result in the inclusion of categories of NFTs in the MiCAR regime in contravention of the express intent of the EU’s co-legislative bodies.

As we previously elaborated in our [response](https://www.esma.europa.eu/press-news/consultations/consultation-reverse-solicitation-and-classification-crypto-assets#responses) to ESMA, because NFTs are formally outscoped from MiCAR, they should not be included in the draft guidelines. In addition to this general concern, we also hold specific concerns about ESMA’s guidelines on the classification of NFTs, particularly with ESMA’s suggestion that NFTs “that are issued ‘in a large series or collection’ may be considered fungible and thereby covered by MiCAR.”[[7]](#footnote-6) Whether a token is non-fungible is a nuanced concept and one that deserves significant attention and clarifying legislative action before regulators develop prescriptive rules on the issue. NFTs in a series generally retain their non-fungibility: trading card NFTs (representing, for instance, a football team) may be issued in a large series or collection, but each individual NFT retains its non-fungibility by, for example, representing different team members or different years of the team. The misclassification of NFTs in such a series as being fungible could be avoided with a principles-based approach, outlined in our [response](https://www.esma.europa.eu/press-news/consultations/consultation-reverse-solicitation-and-classification-crypto-assets#responses) to ESMA and summarised below, which would assess each NFT in a series on its own merits.

Likewise, value interdependency (as covered in ESMA’s draft guidelines) is a weak indicator of fungibility. Although NFTs in a series may have interdependent value because of the perceived value of a collection as a whole, NFTs do not become fungible on that basis. Rather, as is the case with their physical analogs, buyers and sellers commonly value different traits, attributes, or types of NFTs within a collection differently, despite ascribing general value to the collection as a whole. In addition, some traits may provide special or additional utility, so while a given NFT’s value may be connected to the larger series, the NFT itself remains unique. For example, the value of one NFT in a sports team series (e.g., an NFT representing the goalie) may have some correlation to the value of another NFT in that series (e.g., NFTs representing the midfielders), but that does not make these NFTs fungible. Another analog from the art world is the concept of limited edition prints or series. When an artist like LeRoy Neiman creates a series of lithographs in a subject area such as the Olympics or golf, his offering multiple copies of prints within that topic area does not convert his artwork into a fungible instrument. Indeed, value interdependence should have little, if any, bearing on whether assets are non-fungible. Here too, a principles-based approach is crucial.

We are also concerned about ESMA’s conditions and criteria related to fractionalised NFTs, as well as the ESAs’ draft guidelines reference to MiCAR’s Recital 11. In paragraph 73 of its guidelines, ESMA states that “Fractional parts of a unique and non-fungible crypto-asset should not be considered unique and non-fungible.”[[8]](#footnote-7) However, in paragraph 140 of these draft guidelines, ESMA implies that “fractional parts of a unique and non-fungible crypto-asset, when considered separately” may be “deemed unique and non-fungible.”[[9]](#footnote-8) As a starting point, we strongly recommend that ESMA clarify these apparently contradictory statements. In line with our foregoing comments, we also urge the ESAs to guide NCAs to avoid an overbroad position with respect to fractionalised NFTs, and instead to use the principles-based approach explained below for appropriately categorising them based on their intended and predominant uses.

To avoid these issues the ESAs should recommend the use of a principles-based approach to NFT classification. As explained in our response to ESMA, outside of MiCAR, NCAs should be directed to use a principles-based approach for NFT classification. Principles-based approaches are important when it comes to emerging technology which evolves so quickly that regulators cannot prescribe their way to pragmatic outcomes; principles-based approaches can best help authorities achieve their objectives in rapidly evolving spaces.

Such a principles-based approach should focus on assessing the intended use of the NFT and how market participants primarily use it. If an NFT represents ownership in a good or service, the NFT should be regulated as the good or service would typically be; identifying an asset as an NFT should not alter its regulatory treatment. To that end, a “look-through” analysis is a reasonable approach. For instance, if an NFT provides its holder with access to a membership club with the NFT acting as a membership card — the regulatory treatment would focus on the club membership. Critically, unlike utility tokens, NFTs provide *unique* access — in the case of the membership club NFT, for a specific member to a unique club. In this example, a single right is associated with the NFT.

In the case that an NFT has multiple associated rights, goods, or services, we believe that NCAs be advised to apply the “look-through” analysis in combination with intended use and predominant purpose approaches. For example, it is possible that the membership club NFT could provide the holder of the NFT not only with access rights to a club, but also with a right to attend an exclusive event. In such a case, a “look-through” analysis absent a predominant purpose or intended use approach would require rules to determine how to value the NFT based on an allocation among the different associated rights or assets, which could result in costly appraisals. But a “look-through” analysis combined with these approaches diminishes complexity while encouraging innovation. We also recommend that NCAs be advised that an NFT’s use can be manifold and may change over time, so classifications may need to be revised. While it is conceivable that bad actors could attempt to circumvent MiCAR regulations by issuing fungible assets in the guise of an NFT series, we believe that this principles-based approach to classifying NFTs would uncover this and preserve the integrity of the NFT market without generically identifying broad categories of NFTs as non-fungible and subject to MiCAR.

We are hopeful that ESMA will incorporate this feedback in the final version of its Guidelines, but wish to reiterate these points here for the ESAs, given that the Consultation Paper made reference to the ESMA guidelines, as well as to MiCAR’s Recital 11.

1. **Start-up exemption**

We appreciate MiCAR’s aim of supporting innovation and fair competition, while also ensuring a high level of protection for retail holders and the integrity of markets in crypto-assets. To that end, we strongly agree with MiCAR that “SMEs and start-ups should not be subject to excessive and disproportionate administrative burdens,” and thus support the exemption included in MiCAR for SMEs and start-ups.[[10]](#footnote-9) However, we believe that the maximum consideration threshold for this exemption is too low to avoid subjecting startups to excessive and disproportionate administrative burdens. We therefore recommend that the ESAs raise the maximum consideration threshold from EUR 1 000 000 over a period of 12 months to EUR 5 000 000 over 12 months.

As the Consultation Paper notes, these draft Guidelines may create additional costs for prospective issuers, offerrors, and persons seeking admission to trading based on the data and information that must be provided to the competent authorities to remain compliant. We believe that these costs would be disproportionately burdensome for startups pioneering novel technologies and business models. For small businesses, the need to undergo the standardised test and in some cases comply with the full breadth of MiCAR’s relevant requirements may be extremely burdensome. Therefore, we recommend that the ESAs extend the aforementioned start-up exemption to offers whose total consideration does not exceed EUR 5 million over a period of 12 months.

1. European Parliament and Council, *Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937* (May 31, 2023), <https://eur-lex.europa.eu/eli/reg/2023/1114/oj> [Hereinafter: MiCAR]. [↑](#footnote-ref-0)
2. ESAs, *Consultation on Guidelines on templates for explanations and opinions, and the standardised test for the classification of crypto-assets under MiCAR: Consultation on Guidelines on templates for explanations and opinions, and the standardised test for the classification of crypto-assets under MiCAR form* (July 12, 2024), <https://www.eba.europa.eu/publications-and-media/events/consultation-guidelines-templates-explanations-and-opinions-and-standardised-test-classification> [Hereinafter: Consultation Paper]. [↑](#footnote-ref-1)
3. ESMA, *On the draft Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments* (Jan. 29, 2024), [https://www.esma.europa.eu/sites/default/files/2024-01/ESMA75-453128700-52\_MiCAR\_Consultation\_Paper\_-\_Guidelines\_on\_the\_qualification\_of\_crypto-assets\_as#\_financial\_instruments.pdf](https://www.esma.europa.eu/sites/default/files/2024-01/ESMA75-453128700-52_MiCA_Consultation_Paper_-_Guidelines_on_the_qualification_of_crypto-assets_as_financial_instruments.pdf) [Hereinafter: ESMA guidelines]. [↑](#footnote-ref-2)
4. “[...] MiCAR applies to crypto-assets that are not: unique and non-fungible with other crypto-assets” Consultation Paper at 4. [↑](#footnote-ref-3)
5. Article 2 of MiCAR states that: “This Regulation does not apply to crypto-assets that are unique and not fungible with other crypto-assets.” [↑](#footnote-ref-4)
6. Consultation Paper at16. [↑](#footnote-ref-5)
7. ESMA guidelines, at 37. [↑](#footnote-ref-6)
8. *Id.* at 21. [↑](#footnote-ref-7)
9. *Id.* at 37. [↑](#footnote-ref-8)
10. Recital 27 of MiCAR states that: “SMEs and start-ups should not be subject to excessive and disproportionate administrative burden. Accordingly, offers to the public of crypto-assets other than asset-referenced tokens or e-money tokens in the Union whose total consideration does not exceed EUR 1 000 000 over a period of 12 months should also be exempt from the obligation to draw up a crypto-asset white paper.” [↑](#footnote-ref-9)