| Reply form  on the Consultation Paper on guidelines on conditions and criteria for the classification of crypto-assets as financial instruments for MiCA implementation |
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## 

**Responding to this paper**

ESMA invites comments on all matters in this consultation paper and in particular on the specific questions. Comments are most helpful if they:

* respond to the question stated;
* indicate the specific question to which the comment relates;
* contain a clear rationale; and
* describe any alternatives ESMA should consider.

ESMA will consider all comments received by **29 April 2024.**

**Instructions**

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the below steps when preparing and submitting their response:

1. Insert your responses to the questions in the Consultation Paper in the present response form.
2. Use this form and send your responses in Word format (**pdf documents will not be considered except for annexes**);
3. Please do not remove tags of the type <ESMA\_QUESTION \_MIC3\_1>. Your response to each question has to be framed by the two tags corresponding to the question.
4. If you do not wish to respond to a given question, please do not delete it but simply leave the text “TYPE YOUR TEXT HERE” between the tags.
5. When you have drafted your response, name your response form according to the following convention: ESMA\_MIC3\_nameofrespondent\_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA\_MIC3\_ABCD\_RESPONSEFORM.
6. Upload the form containing your responses, **in Word format**, to ESMA’s website (www.esma.europa.eu under the heading “Your input – Open Consultations” -> Consultation Paper on guidelines on conditions and criteria for the classification of crypto-assets as financial instruments”).

**Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publically disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA’s rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA’s Board of Appeal and the European Ombudsman.

**Data protection**

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading [Legal Notice](http://www.esma.europa.eu/legal-notice).

**Who should read this paper**

# All interested stakeholders are invited to respond to this consultation paper. In particular, ESMA invites crypto-assets issuers, crypto-asset service providers and financial entities dealing with crypto-assets as well as all stakeholders that have an interest in crypto-assets.

**General information about respondent**

| Name of the company / organisation | Ozone Networks, Inc. d/b/a OpenSea |
| --- | --- |
| Activity | Non-Financial Counterparty |
| Are you representing an association? | ☐ |
| Country/Region | United States |

The Honorable Chair Verena Ross

ESMA

201-203 rue de Bercy

CS 80910

75589 Paris Cedex 12, France

Dear Chair Ross,

Ozone Networks, Inc., d/b/a OpenSea (“OpenSea”), welcomes the opportunity to submit these comments in response to the consultation “On the draft Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments” (the “Guidelines”), which the European Securities and Markets Authority (“ESMA”) issued on 29 January, 2024. In particular, our comments address question six regarding the “Classification as crypto-assets which are unique and not fungible with other crypto-assets (NFTs)”. We believe that clarifying the position of which non-fungible tokens (“NFTs”) are to be in scope of the Markets in Crypto Assets Regulation (“MiCA”) is essential to the future growth of NFTs and the greater web3 economy worldwide. In particular, while we agree that MiCA should not apply to crypto-assets that are unique and not fungible with other crypto-assets, we believe the guidelines should make clear that the vast majority of non-financial NFTs are outside the scope of MiCA. In place of the proposed test for uniqueness and non-fungibility, we suggest implementing a look-through analysis to identify the associated right or asset of an NFT and whether or not it is financial in nature.

***The OpenSea Web3 Marketplace***

OpenSea is the world’s foremost non-custodial explorer and web3 marketplace for NFTs. We are helping the world’s creators and collectors own and shape their relationships directly with their communities, and we believe NFTs are central to the open, interoperable data infrastructure created by blockchains that will allow for this paradigm shift. We are focused on providing a trusted, inclusive, peer-to-peer platform and tools that can help creators and collectors access web3 and explore, create, buy, and sell NFTs on public blockchains.

**Questions**

1. **Do you agree with the suggested approach on providing general conditions and criteria by avoiding establishing a one-size-fits-all guidance on the concepts of financial instruments and crypto-assets or would you support the establishment of more concrete condition and criteria?**

<ESMA\_QUESTION\_MIC3\_1>

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<ESMA\_QUESTION\_MIC3\_1>

1. **Do you agree with the conditions and criteria to help the identification of crypto-assets qualifying as transferable securities? Do you have any additional conditions and/or criteria to suggest? Please illustrate, if possible, your response with concrete examples.**

<ESMA\_QUESTION\_MIC3\_2>

TYPE YOUR TEXT HERE

<ESMA\_QUESTION\_MIC3\_2>

1. **Based on your experience, how is the settlement process for derivatives conducted using crypto-assets or stablecoins? Please illustrate, if possible, your response with concrete examples**

<ESMA\_QUESTION\_MIC3\_3>

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<ESMA\_QUESTION\_MIC3\_3>

1. **Do you agree with the conditions and criteria to help the identification of crypto-assets qualifying as another financial instrument (i.e. a money market instrument, a unit in collective investment undertakings, a derivative or an emission allowance instrument)? Do you have any additional conditions, criteria and/or concrete examples to suggest?**

<ESMA\_QUESTION\_MIC3\_4>

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<ESMA\_QUESTION\_MIC3\_4>

1. **Do you agree with the suggested conditions and criteria to differentiate between MiFID II financial instruments and MiCA crypto-assets? Do you have concrete conditions and/or criteria to suggest that could be used in the Guidelines? Please illustrate, if possible, your response with concrete examples.**

<ESMA\_QUESTION\_MIC3\_5>

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<ESMA\_QUESTION\_MIC3\_5>

1. **Do you agree with the conditions and criteria proposed for NFTs in order to clarify the scope of crypto-assets that may fall under the MiCA regulation? Do you have any additional conditions and/or criteria to suggest? Please illustrate, if possible, your response with concrete examples.**

<ESMA\_QUESTION\_MIC3\_6>

Under the published Guidelines, ESMA determined that “Non-Fungible Tokens (NFTs) which cumulatively meet the criteria of uniqueness and non-fungibility remain exempt from MiCA”[[1]](#footnote-0). To evaluate each NFT’s “uniqueness and non-fungibility”, the Guidelines emphasize looking past “specific technical identifiers or standards” in favor of assessing the value interdependency and interchangeability of each NFT. This holistic, case-by-case evaluation will be conducted by each National Competent Authority (NCA), which will be charged with determining whether an NFT is sufficiently “unique and not fungible with other crypto-assets”.[[2]](#footnote-1)

As an initial matter, we agree that NFTs merit a case-by-case approach to determine whether they may fall under the MiCA regulation. However, we disagree with the proposed conditions and criteria that: (1) the technical features and standards used to define NFTs should not be of “primary importance to NCAs” when making its determinations; (2) value interdependence that may exist between NFTs is a key aspect indicating a lack of uniqueness, and; (3) NFTs, especially those in a series or collection, that share equivalent characteristics are interchangeable and thus fungible, and; 4) fractional NFTs are not to be considered unique and non-fungible. In place of the proposed factors to assess an NFT’s uniqueness and fungibility, we suggest NCAs should use a look-through analysis that identifies (in instances where the NFT is associated with an item/file/asset) what the NFT is associated with, and whether it is a financial or non-financial use-case. As the European Parliament correctly suggested when excluding NFTs from MiCA, the majority of NFTs are non-financial in nature and should be outside of the scope of this regulation.

***About NFTs***

Prior to responding to ESMA’s proposed conditions and criteria for the treatment of NFTs, we would like to provide further background on NFTs. NFTs are identifiable data units within a data infrastructure (*i.e.,* blockchain). Each NFT has a unique token ID (which cryptocurrencies do not have) that can be used to track its individual transaction history, and most NFTs have links to a URL that contains NFT metadata. That metadata may include one or more URLs to a digital file, most commonly an image. If the NFT links to an image, the image is usually the “face” of the NFT when it is displayed by apps that assist users to explore NFTs. Additionally, so long as the blockchain the NFT “lives” on is public, the provenance and ownership history of the NFT are publicly available.

The NFT metadata and any linked digital file are populated by the NFT creator. Together, they can certify authenticity, convey ownership or licensing rights, serve as a credential or identity verification, provide redemption rights for intangible or tangible things, and more.

The following list includes the most common examples of current NFT use cases:

* **Digital Art NFTs:** Broadly, digital art NFTs are associated with all types of digital images, including drawings, paintings, graphic art, photography, video art, and generative art.
* **Trading Card/Fan NFTs:** trading card NFTs feature a digital image of individual athletes, teams, or fictional figures (*e.g.,* popular cartoons). Similarly, there are NFTs associated with commemorative memorabilia that allow fans/supporters of a particular athlete, team, or figure to own and display memorabilia.
* **Music NFTs:** Artists can associate an NFT with content by linking to a digital audio file and adding metadata, such as the name of the artist or band, the song title, and the genre.
* **Redeemables (*e.g.,* Fashion, Luxury Goods, Beauty):** Some NFTs can be redeemed for a physical item. For example, an NFT may give its owner the right to claim a pair of sneakers or a bottle of wine.
* **Membership/Ticket NFTs:** NFTs can be used to allow access to events, materials, specific content, community resources, or other perks. Membership NFTs are also used for consumer loyalty programs.
* **Identity/Credential NFTs:** Due to the unique nature of identity NFTs, individuals can use them validate their identities in a way that limits the need for disclosure of personally identifiable information. NFTs can also be used for protected recordkeeping.
* **Domain Name NFTs:** NFTs can serve as a “vanity plate” or domain name for a user’s crypto wallet address, such that ownership of the NFT in a particular wallet means the crypto wallet address will specifically be associated with that domain name (similar to a URL redirect).
* **Financial Instrument/Investment or Payment NFTs:** NFTs can be used to represent ownership over financial instruments like stocks, bonds, and financial contracts. NFTs can also be used for payment purposes (like currency) when they are redeemable for or serve as a store of value or medium of exchange. For instance, NFTs can be associated with assets/files/items that represent ownership of cryptocurrencies or NFTs that are redeemable for cryptocurrencies. Currently, there are not many active use cases for NFTs that fall into this category.

In addition to recognizing the existing use-cases for NFTs that fall under these categories, it is important to recognize that NFTs may convey multiple rights, including ownership and legal rights, and/or be associated with multiple assets. For example, an NFT can function as a concert ticket prior to an event and digital art memorabilia following the concert. As the technology continues to develop, we may see an increasing number of multi-purpose NFTs that fit under a wide variety of use-cases.

***Discussion***

*Technical Standards*

While NFTs’ technical features (e.g., token identification code, unique token ID, token standard) should not be dispositive of an NCA’s determination regarding a token’s uniqueness and non-fungibility, we disagree with the notion that these technical standards are not of “primary importance… when assessing the fungibility and uniqueness of [a] crypto-asset”[[3]](#footnote-2).

Ascertaining whether a token has a unique token ID and metadata, as well as the rights that metadata conveys to its owner, is highly relevant to determining whether the token should be considered as a NFT or a crypto-asset subject to MiCA’s requirements. Additionally, current and developing NFT token standards (e.g., ERC-721 and ERC-1155) function differently and may affect the value of ownership or the manner in which you can transfer these tokens. The technical identifiers and standards, while not acting as the sole identifiers for if a token is unique and non-fungible, are crucial components that should be given appropriate weight in any analysis conducted by an NCA.

*Value Interdependence*

The Guidelines propose to determine the uniqueness of a NFT based on: (1) the intrinsic connection between an NFT’s value and its individual attributes and specific utility it confers to the holder, and (2) the extent to which value interdependence exists between NFTs. Further, ESMA suggests that the “notions of uniqueness and fungibility within the meaning of MiCA seemed to be detached from that of negotiability on a secondary market”, indicating that value interdependence will not be assessed based on secondary market sales.

We agree with the Guidelines stating “for a crypto-asset to be considered unique, its value should be intrinsically connected to its individual attributes and the specific utility it confers to its holder”[[4]](#footnote-3). We believe that the individual attributes, specific utility, and features of any given NFT should be the largest factors in determining whether an NFT is “unique” and “non-fungible”. Further, we agree that uniqueness and non-fungibility should be detached from negotiability on a secondary market; while secondary markets may reveal demand for a certain product, the activities of buyers and sellers does not indicate whether the NFT itself is “unique” or “non-fungible”.

However, we disagree with the assertion that whether “the valuation of one crypto-asset influences the valuation of another” is a “key aspect” that should be considered in determining whether an NFT is sufficiently unique.[[5]](#footnote-4) For the majority of use-cases, the value of NFTs, like other collectible items (e.g., digital artwork, trading cards, etc.), often fluctuates based on non-material factors, as ESMA itself acknowledges[[6]](#footnote-5). To use the same analogous situation highlighted in the Guidelines, famous artists and painters tend to have the ability to sell their works at higher prices, irrespective of the aesthetic or material attributes of the work. These artists' works also tend to fluctuate in value depending on external factors that may be completely outside the control of the creator. These works are largely considered unique and non-fungible, despite exhibiting interdependent value and being influenced by non-material factors. It is for this reason that relying on value interdependency between NFTs as a “key aspect” for determining uniqueness is, at the very least, misleading–there are many reasons why NFTs may move together in value that may or may not be related to the “uniqueness” of the item. We thus caution ESMA against placing too much emphasis on the significance of value interdependence in issuing its final Guidelines, and suggest the case-by-case analysis focus on the individual attributes and specific utility each NFT grants to its holder.

*Interchangeability*

The Guidelines assert that “NFTs that are part of a series, or a collection can be qualified as crypto-assets in the meaning of MiCA if they are interchangeable”[[7]](#footnote-6). ESMA interprets interchangeable to mean if NFTs share equivalent characteristics in practice, then they will be considered interchangeable and should fall under MiCA.

We strongly disagree with the conclusion that the existence of a collection or series should automatically be equated with fungibility. Moreover, the example ESMA itself gives– i.e., “in scenarios where the market views certain NFTs as having similar value despite unique attributes”--proves the point[[8]](#footnote-7). As previously stated related to ESMA’s identification that secondary market negotiability is detached from the notions of uniqueness and fungibility, the market simply identifies the existence and interest of buyers and sellers, not whether the NFT itself is unique or non-fungible.

Further, NFTs are not interchangeable in the same way that crypto-assets are. For example, cryptocurrencies like Ethereum and Bitcoin are readily interchangeable for themselves, where exchanging one Bitcoin for another Bitcoin transfers identical value and utility to both parties, without needing an intermediary or conversion prior to exchange. The same cannot be said for the majority of NFTs, in large part because of their unique attributes and subjective value. For example, trading cards, both physical and digital, are often issued as part of a series or collection and typically unique in terms of the images they represent. However, granted the trading cards are not identical, these items are not interchangeable in the same manner as the crypto-assets covered under MiCA. Regardless of their value, collectors and purchasers of digital trading cards and other collection based NFTs are typically resistant to exchanging their item for a similarly priced but different item from the same collection. The vast majority of NFTs are not *readily* interchangeable, regardless of whether they are part of a series/collection or issued individually; the exchange of NFTs resembles the sale and trade of physical items more than the exchange of stores of value like crypto-assets and forms of money.

*Fractional NFTs*

The Guidelines state “fractional parts of a unique and non-fungible crypto-asset should not be considered unique and non-fungible” under the premise that each fractional NFT possesses identical attributes and is “inherently devoid of uniqueness”[[9]](#footnote-8). Functionally, this means all fractional NFTs will be covered under MiCA, irrespective of other factors.

We disagree with the notion that fractional NFTs should not be considered unique and non-fungible solely for the reason that they are fractionalized. Rather, we believe that fractional NFTs should be considered in the same manner as all other NFTs and held to the same standards to determine whether they fit under MiCA. We encourage ESMA to clarify in its final Guidelines that fractionalization is not itself determinative of uniqueness or fungibility.

***Look-Through Analysis***

Consistent with the Guidelines’ approach, we agree with ESMA that a case-by-case analysis is appropriate for determining how best to categorize NFTs. However, rather than instituting a test for “uniqueness and non-fungibility” by assessing perceived value interdependence, interchangeability, and material utility, we believe that ESMA should institute a look-through analysis to identify the associated right/item, its utility, and whether the NFT is financial or non-financial in nature. We believe instituting this process will properly identify tokens that should be covered under MiCA, allow for flexibility in classification as the space continues to develop, and help create consistency between NCAs in determining the proper classification.

ESMA should institute a look-through analysis, in place of the proposed test for uniqueness and non-fungibility, to determine the predominant purpose and use of the NFT, and whether the NFT is financial or non-financial in nature. With a look-through analysis, NCA’s would be tasked to identify the file/image/asset associated with the NFT, and whether the use-case is financial in nature. Where an NFT represents ownership of an item, the NFT should be treated as that item for regulatory purposes. Where an NFT conveys multiple rights, the look-through analysis should seek to determine what the NFT’s primary purpose is, which in some cases can be identified in the NFT’s metadata itself. In instances where the NFT and associated item is financial in nature (e.g., tokenized securities, real-estate, financial instruments), the NFT should be covered under MiCA or MiFID. If the NFT is not financial in nature, the NFT should be outside the scope of MiCA, which is inline with MiCA’s determination that, due to certain features that limit the extent of their financial use, NFTs have limited risk to holder and the financial system, thus justifying their exclusion from the scope of MiCA.[[10]](#footnote-9) This separation of financial and non-financial NFTs is both in-line with the drafting intention of MiCA, while capturing the financial tokens under the proper regime.

<ESMA\_QUESTION\_MIC3\_6>

1. **Do you agree with the conditions and criteria proposed for hybrid-type tokens? Do you have any additional conditions and/or criteria to suggest that could be used in the Guidelines?  Please illustrate, if possible, your response with concrete examples.**

<ESMA\_QUESTION\_MIC3\_7>

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<ESMA\_QUESTION\_MIC3\_7>

1. 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_MiCA_Consultation_Paper_-_Guidelines_on_the_qualification_of_crypto-assets_as_financial_instruments.pdf> [Hereinafter: ESMA Consultation Paper]. [↑](#footnote-ref-0)
2. *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/legal-content/EN/TXT/?uri=CELEX%3A02023R1114-20240109> [Hereinafter: MiCA] Art. 2(3). [↑](#footnote-ref-1)
3. ESMA Consultation Paper, par. 68. [↑](#footnote-ref-2)
4. ESMA Consultation Paper, par. 69. [↑](#footnote-ref-3)
5. ESMA Consultation Paper, par. 68. [↑](#footnote-ref-4)
6. ESMA states that there are “instances where genuine NFTs will exhibit value correlation precisely because of their common features - such as the same author, as is the case with art in the real world.” [↑](#footnote-ref-5)
7. ESMA Consultation Paper, par. 70. [↑](#footnote-ref-6)
8. Ibid. [↑](#footnote-ref-7)
9. ESMA Consultation Paper, Footnote par. 73. [↑](#footnote-ref-8)
10. *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> Rec. 10. [↑](#footnote-ref-9)