Ava Labs.
1177 Avenue of the Americas, 5th Floor
New York, NY 10036

Owl Explains' Public Comment on IMF-FSB Synthesis Paper: "Policies for Crypto-Assets"

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Secretariat to the Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Submitted Via Email: fsb@fsb.org

To whom it may concern:

Owl Explains appreciates the opportunity to comment on the recent paper entitled "IMF-FSB Synthesis Paper: Policies for Crypto-Assets" (the "Joint Paper"). The Joint Paper brings together in one place work that both organizations have undertaken regarding crypto-assets, including findings from IMF work on macroeconomic and monetary issues and FSB work on financial stability.

Owl Explains is a project led by the legal team at Ava Labs, Inc. that aims to support workable regulation of blockchain and crypto-assets (also called "tokens") through a set of guiding principles known as the Tree of Web3 Wisdom — and a system for determining the legal and regulatory treatment of crypto-assets according to their true nature (functions and features) known as the sensible token classification system. More information about the initiative appears at the end of this letter.

The Joint Paper's stated goal was to combine recommendations concerning macroeconomic and monetary issues and recommendations related to financial stability into a single, comprehensive set of policy considerations. The paper outlines key regulatory challenges and highlights the need for "[a] comprehensive policy and regulatory response for crypto-assets . . . ." We agree with the overall theme of implementing workable regulations that focus on the areas of macroeconomic and monetary policy and financial stability. We also applaud the goals of market integrity and investor protection through global coordination, as reflected in our article here.

We believe, however, that the Joint Paper and its associated recommendations would benefit from greater acknowledgement of and discussion about the following core points about blockchain and tokenization:

- Crypto-assets (tokens) are not all the same. They are not a homogenous asset class.
- This is true because tokens are digital representations of assets, items and things and therefore can represent anything.
- Accordingly, tokens cannot all be treated the same under law and regulation, or for macroprudential and financial stability purposes.
- Many tokens represent assets, items or things that are already subject to the standards and recommendations of the Joint Paper, and are regulated accordingly.
- Many other tokens represent items that are not regulated in the non-blockchain world because they do not require it and so should not be regulated simply because they are tokenized on a blockchain.
- Accordingly, broad definitions of crypto-assets such as the one in the Joint Paper may result in more confusion than clarity.

Blockchain is a new technology, but in essence it is simply a new kind of database or filing cabinet. When it comes to law and regulation, treating all crypto-assets the same simply because they are tokenized representations recorded on a blockchain makes as little sense as treating a sketch, an ID card, a receipt or a share certificate all the same because they are printed on paper and filed in the same filing cabinet.

Instead, policymakers and regulators should treat each token according to what it actually represents - just as they do with things written on paper. By looking at a crypto-assets functions and features, we can determine its utilization, valuation, and classification (including for legal/regulatory purposes).

The good news is that the majority of tokens represent things that already existed before blockchain and can be treated as legal or illegal, regulated or unregulated just as they always have been. Policymakers should simply scrutinize what the token actually represents - its features, functions and risk profile - and apply existing laws and regulations - or not - accordingly. This way regulation stays consistent across different technologies - same asset, equals same risk, which results in the same legal and regulatory treatment. The same is true in the context of macreconomic, monetary, or financial stability policy.

The Owl Explains sensible token classification system breaks tokens down into the following five high level categories that represent the vast majority of use cases today and into the future:

Physical asset tokens: Any digital representation of a tangible (real-world) asset created and maintained on a blockchain (also known as "DLT" for distributed ledger technology). This category is very broad and could be divided into smaller categories based on the particular type of tangible asset (e.g., gold coin physical asset tokens, Air Jordan physical asset tokens, cup of coffee physical asset tokens versus coffee cup physical tokens, etc.).

Services tokens (includes music, digital art); Any digital representation of services to be provided by one or more persons/entities to other person(s)/entities. This category also includes music and purely digital art files (the intellectual property underlying the music or digital art file may be an intangible asset token, discussed next, if not transferred with the file). This category is also quite broad because it includes any type of services and digital art/music such that it is susceptible to sub-categorization (e.g., cleaning services tokens, personal performance tokens versus concert ticket tokens, legal services tokens, etc.).

Intangible asset tokens: Any traditional intangible (non-physical) asset. Another broad category susceptible to sub-categories based on the asset class (bond tokens [security tokens], intellectual property rights tokens, government program tokens, loyalty points program tokens, etc.).

Native DLT tokens: A narrow category of truly DLT-native tokens (e.g., Bitcoin, Ether, AVAX, etc.). Might be a subset of intangible asset tokens in the sense that these tokens are just a bundle of rights with no physical item involved, although some may have an element of services (e.g., when the token is used for resource allocation on the network). The classification system treats native DLT tokens as not a subset of intangible asset tokens because the latter must be something that exists (or can exist) distinct from the blockchain that creates and maintains it. Native DLT tokens have no existence or purpose without the associated blockchain. This paper by Professor Carla Reyes is instructive.

Stablecoins: A narrow category of tokens that do not fall within any other category and are designed to maintain stable value against some underlying, reference or linked asset or pool/basket of assets. Usually applied to fiat currencies. This category should not be broadened to swallow all the other categories.

Classifying tokens according to this system will be a crucial first step in the implementation of IMF-FSB's recommendations because it will make clear when assets and activities provide true cause of concern from the standpoint of macroeconomic, monetary, or financial stability policy.

We therefore encourage IMF-FSB and all policymakers and regulators to start their activities with reference to the fundamental principles in the sensible token classification system and use its broad categories to orient their efforts.

About Owl Explains

Owl Explains is a project created by the Legal team at Ava Labs with the goal of becoming a trusted educational resource for policymakers, regulators, and other parties interested in learning about blockchain technology, cryptoassets, and Web3. Owl Explains develops content delivered by leading industry experts, including podcasts, explainers, articles, and quizzes, focusing on understanding the technology and the full breadth of its use cases, distinguishing where those use cases fit within existing regulatory frameworks, as well as defining principles for regulation based on the nature of the asset and activity. Innovation is the soil from which we can create a better Internet. Blockchain is its root system: decentralized, transparent, secure, and traceable. We believe that workable regulation in conjunction with innovation and invention is the best way to guide the transformative power of Web3 to empower individuals and businesses, drive economic inclusion, and benefit the planet. As such, the Owl has developed the Tree of Web3 Wisdom, a set of principles to help guide blockchain and crypto regulation worldwide.

Conclusion

We urge IMF-FSB to adopt the principles of the sensible token classification system as part of its work on crypto and digital assets. Treating all tokens the same, particularly as more and more traditional assets are tokenized, is not workable because it is neither technology neutral nor efficient. We would be happy to discuss further.

Sincerely yours,

DocuSigned by:
Lee A. Schneider
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Lee A. Schneider
General Counsel
Ava Labs, Inc.