26.11.2024

NOTICE TO MEMBERS

Subject: Petition No 0699/2024 by O.G. (German) on laws to regulate digital goods marketplaces

1. Summary of petition

This petition calls for laws to regulate marketplaces selling digital goods, such as non-fungible tokens (NFTs). The laws should take account of the environmental consequences as well as the protection of children, young people and those at risk of addiction. In support of this demand, the petitioner writes that the video game industry now also has its sights on the NFT market, giving rising to new dangers and issues. For example, the petitioner claims that it is a common strategy in software development to keep digital goods in short supply, in order to bump up their value and make success in the game dependent on this. Incorporating NFTs in this market would bring whole new dimensions to such processes, and digital objects with the slightest of differences would become one-time products. A dedicated marketplace is already being developed for these, which gives the impression that making money by trading NFTs is easy and also that investments made within gaming communities have a special status. On top of this, influencers operating in this area are sending out the message that it is easy to get hold of rare and unique NFTs; owing to their scarcity, however, these come with horrendous price tags attached. We urgently need to stop NFT market places or in-game economies from turning into unregulated casinos or exchanges. Reference is also made to money laundering – another potential danger zone in which NFTs present new risks.

2. Admissibility

Declared admissible on 14 October 2024. Information requested from Commission under Rule 233(5).

3. Commission reply, received on 26 November 2024

The Commission's observations

The Commission observes that non-fungible tokens (NFTs) form a core element of the emerging Web3, which is based on distributed ledger technology (DLT/"blockchain") that enables a bottom-up, inclusive, data ownership preserving and democratic digital economy to the benefit of citizens and enterprises. NFTs have been thoroughly analysed in the work that led to the Markets in Crypto Assets Regulation (MiCAR) adopted on 31 May 2023[1] and the Communication on virtual worlds adopted on 05 July 2023[2]. As part of the latter Communication a series of use cases were highlighted.[3]

NFTs – as unique digital representations of value recorded on a blockchain – are used to certify ownership and/or authenticity of an underlying asset. This allows for the commercialisation of unique assets, for which it is otherwise difficult to prove ownership and to trade them. It also enables content creators to design entirely new digital product lines and benefit directly from subsequent revenue streams. The result is more control for content creators over the value and the conditions of the sale of their digital creations. Moreover, NFTs form a secure manner to democratise investment by fractionalising real-world assets, such as real estate, commodities and art objects.

Moreover, the Commission based flagship DLT infrastructure projects on NFTs. A primary example is the emerging anti-counterfeiting blockchain infrastructure that will help prevent the import of fake products. In parallel, industrial ecosystems explore NFT-based solutions, including the cultural and creative industries, metaverse-oriented brands within their value chains as well as the energy sector for tokenising green electricity and hydrogen.

The petitioner's remarks, which date from January 2022 and thus precede the above-mentioned Commission work, in which these aspects have been broadly discussed, focuses on certain financial aspects of NFT marketplaces. An NFT can indeed create an economic benefit in monetary terms, but this is usually not its primary function. NFTs are primarily token "containers" transporting sets of rights and obligations frequently associated to real economy activities or intellectual property. This is why the MiCA regulation excluded NFTs from its scope, stating that this regulation should not apply to crypto assets that are unique and not fungible with other crypto assets, including digital art and collectibles, the value of which is attributable to each crypto asset's unique characteristics and the utility it gives to the token holder.[4]

The Commission further observes that the approach taken on MiCA is in line with the principles underlying European regulation, which follows a risk-based approach. The smaller the part of the economy that is to be regulated is in absolute terms and the less systemic any potential risks are, the smaller is the need to design regulation at EU level. Crypto markets, including NFT platforms, are much smaller than other financial and capital markets that are subject to regulation, and the MiCA Regulation is best be seen as proactive regulatory enabler of such markets than a necessity born out of pending risks. This is also why the Commission service in charge has not taken further steps to regulate NFTs.

There are aspects of NFTs that merit reflection, including taxation and energy use. On taxation,

[1] Cf. https://eur-lex.europa.eu/eli/reg/2023/1114/oj.
[2] Cf. https://digital-strategy.ec.europa.eu/en/library/eu-initiative-virtual-worlds-head-start-next-technological-transition.
[3] Cf. https://digital-strategy.ec.europa.eu/en/factpages/virtual-worlds.
[4] The subsequent reflections in the respective MiCA recital that consider exceptional instances where NFTs might become subject of this regulation is no contradiction here, as they refer to tokens that are labelled as NFTs while in fact being crypto assets because of their insufficient uniqueness, meaning that they are NFTs only through misleading labelling but not because of their substance.

the Commission has limited competences but observes market developments and discusses meaningful ways forward. On energy consumption, NFTs are usually based on Ethereum space business models, which in comparison use very little energy per transaction and thus outperform alterative solutions on non-NFT platforms.

The Commission finally notes that the absence of a dedicated NFT regulation does not mean that NFTs fall outside of existing regulatory requirements that apply to economic activity in the platform economy. These of course continue to apply and include the various policy fields as mentioned in the petition. Pending future evidence to the contrary, the Commission therefore considers the current treatment of NFTs on digital platforms as adequate.

Conclusion

A thorough assessment by the European Commission in the context of the MiCA Regulation, the Virtual World Communication and real economy blockchain infrastructures has concluded that, when applying a risk-based approach, neither the size of NFT marketplaces nor their limited risk potential merit further regulation. Remaining risks are currently effectively addressed based on existing legislation. As such, the European Commission does not see a need to change its pro-innovation approach on NFTs unless further analyses were to provide solid evidence to the contrary.