

Comment Intake—LP Payment Applications Rulemaking
Consumer Financial Protection Bureau
c/o Legal Division Docket Manager
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VIA EMAIL AND FEDERAL REGISTER

January 8, 2024

Re: a16z’s Comments to Proposed Rule Defining Larger Participants of a Market for General-Use Digital Consumer Payment Applications (Docket No. CFPB-2023-0053 or RIN 3170-AB17)

Dear Director Chopra:

Andreessen Horowitz (“a16z”) appreciates the opportunity to respond to the Consumer Financial Protection Bureau’s (the “Bureau”) request for comment on “Defining Larger Participants of a Market for General-Use Digital Consumer Payment Applications,” published on November 17, 2023 (the “Proposed Rule”).¹ We appreciate the Bureau’s efforts to assess compliance with federal consumer financial law and detect potential risks to consumers in novel markets, such as digital assets. In addition to the comments provided below, we would welcome an opportunity to meet with you and your staff to answer any questions that you may have and discuss our comments below in more detail.

As an initial matter, we note that the scope of the Proposed Rule has the potential to, perhaps unintentionally, encompass providers or developers of technologies that are not directly involved in transferring funds or executing transactions, as well as transactions in assets that do not constitute funds under the Consumer Financial Protection Act (“CFPA”). Our comment letter focuses on two examples in particular: transactions involving certain fungible digital assets and non-fungible tokens (“NFTs”), as well as self-hosted digital asset wallets (also known as non-custodial wallets). We provide a brief overview of each below, and we explain why they should not fall within the scope of the Proposed Rule. We conclude with a request that, in future iterations of the Proposed Rule, the Bureau clarify that the Proposed Rule does not extend to all transactions involving digital assets and self-hosted wallets.

I. About a16z

A16z is a venture capital firm that invests in seed, venture, and late-stage technology companies, focused on bio and healthcare, consumer, crypto, enterprise, fintech, and games. A16z currently has more than \$35 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

¹ CFPB, “Defining Larger Participants of a Market for General-Use Digital Consumer Payment Applications” 88 Fed. Reg. 80,197, at 80,202 (Nov. 17, 2023) (Proposed Rule).

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 on short-term crypto-asset price fluctuations.

At a16z, we believe we need an Internet that can foster competition and mitigate the dominance of large technology companies, unlock opportunities in the innovation economy, and enable people to take control of their digital information. The solution is web3 — the third generation of the Internet — a group of technologies that encompasses blockchains, digital assets, decentralized applications and finance, and decentralized autonomous organizations. Together, these tools enable new forms of human collaboration that can help communities make better collective decisions about critical issues, such as how networks will evolve and how economic benefits will be distributed. We are optimistic about the potential of web3 to strengthen trust in institutions and expand access to opportunity.

II. Legal Framework of the Proposed Rule Applied to Digital Asset Transactions

As drafted, the Proposed Rule could extend the Bureau’s supervisory authority to providers of a “covered payment functionality”² through a “digital application” for consumers’ “general use”³ in making “consumer payment transactions.”⁴ Such providers must also meet the transaction threshold to be “larger participants.”⁵ As mentioned above, without further clarity from the Bureau, these definitions identify an overly broad market for supervision, potentially covering providers that are not directly involved in the facilitation of consumer payment transactions, as well as conduct that does not fall within the scope of consumer payment transactions. We note that the discussion below operates with the understanding that certain technologies and market participants in the blockchain ecosystem do not fall within the scope of the Proposed Rule.⁶

A. Transactions involving digital assets

The Proposed Rule is unclear as to which types of digital asset transactions fall within the definition of “consumer payment transactions.” As noted in the Proposed Rule, the first component of the definition of a “consumer payment transaction” is that the payment transaction must result in a transfer of “funds,” which the Proposed Rule interprets to include: “digital assets that have monetary value and are readily useable for financial purposes, including

² See § 1090.109(a)(2) (“Covered payment functionality” includes “wallet functionality,” which means a product or service that (1) stores account or payment credentials, including in encrypted or tokenized form; and (2) transmits, routes, or otherwise processes such stored account or payment credentials to facilitate a consumer payment transaction.).

³ *Id.* (“General use” means that the provider does not impose significant limitations on the purpose of consumer payment transactions that the covered payment functionality facilitates.).

⁴ *Id.* (“Consumer payment transaction” means, subject to certain exceptions, the transfer of funds by or on behalf of a consumer to another person primarily for personal, family, or household purposes.).

⁵ See § 1090.109(b) (“Larger participants” are nonbank entities that provide an annual covered consumer payment transaction volume of at least five million transactions and that were not, during the preceding calendar year, a small business concern.).

⁶ Such technologies and market participants include node operators, validators, and decentralized protocols, among others, which do not provide consumer payment transactions, just as the Bureau does not regulate payment infrastructure rails like SWIFT.

as a medium of exchange.” This interpretation is overly broad and could be subject to challenge under the Administrative Procedure Act and the Fifth Amendment.

First, the Bureau could exceed its statutory authority under the CFPA with the Proposed Rule’s interpretation of “funds.” Because the CFPA does not include a specific definition for “funds,” the Bureau interprets the term with reference to its plain meaning, as well as to five federal court findings relating to digital currency activities under criminal money laundering and Bank Secrecy Act provisions. The cases, according to the Proposed Rule, hold that “certain crypto-assets, including bitcoin, constitute ‘funds’ for purposes of other Federal statutes,” which suggests that at least one digital asset, in addition to bitcoin, is within the scope of “funds” under more than one statute. Given that the cited cases involve only narrow interpretations under Titles 18 and 31 of the United States Code, designation of digital assets as funds under the Proposed Rule is overbroad. Indeed, the case law cited does not support such a broad conclusion — four of the five cited cases relate to bitcoin alone, while the fifth case relates to a digital currency known as e-gold, which pre-dates blockchain-based cryptographic assets. Specifically, the cases interpret the term “funds” under Title 18 in the context of money laundering and the Bank Secrecy Act.⁷ In light of these facts, we respectfully suggest that the Proposed Rule, if adopted, should provide a more specific and narrower interpretation of “funds.”

We also note that in determining how courts have interpreted the term “funds,” the Bureau should have also considered how courts have classified digital assets themselves under other laws besides Title 18. Importantly, the Bureau did not consider cases that have found digital assets to be securities under the Securities Act of 1933 or commodities under the Commodity Exchange Act of 1936. The Bureau is expressly required by statute to coordinate with the Securities and Exchange Commission (“SEC”) and Commodity Futures Trading Commission (“CFTC”) “to promote consistent regulatory treatment of consumer financial and investment products and services.”⁸ While we note that the Proposed Rule would exclude “transfers of funds the primary purpose of which is the purchase or sale of a security or commodity,”⁹ cannot apply to persons regulated by the SEC or CFTC,¹⁰ and makes a passing reference to consultation with the SEC and CFTC,¹¹ it is unclear that the Bureau has fulfilled its coordination obligation, especially given unresolved legal questions regarding which cryptocurrency tokens may or may not be “securities” or “commodities.”

In addition, the Bureau did not account for the wide range of digital assets that share few characteristics with bitcoin. There are thousands of digital assets, many with highly tailored use cases and characteristics, so even if bitcoins were to fall within the scope of “funds” under the CFPA, it does not follow that the Bureau has limitless jurisdiction over digital assets that “have monetary value and are readily useable for financial purposes.” Therefore, without express

⁷ For example, under FinCEN’s statutory authority and guidance, not all digital assets are convertible virtual currency or “value that substitutes for currency.” That determination is made on a facts and circumstances basis for each asset, and more importantly, each activity involving the asset. We recommend that digital assets that may come under the purview of this Proposed Rule should be evaluated similarly.

⁸ 12 USC § 5495 (requiring “coordination” (not just consultation) with the SEC and CFTC, among other regulators).

⁹ Proposed Rule, at 80,203; *see* 12 C.F.R. § 1005.3(c)(4).

¹⁰ 12 USC §§ 5481(20-21); 12 USC §§ 5517(i-j).

¹¹ Proposed Rule, at 80,199.

legislative directive, we caution the Bureau against asserting expansive jurisdiction over digital assets lest it wrongfully assert jurisdiction over some digital assets that are also securities or commodities or otherwise apply that definition inconsistently. Doing so could result in significant confusion with respect to regulatory jurisdiction in the digital asset markets, above and beyond the current perplexing state of affairs.

Second, the Bureau's interpretation of "funds" is vague without further guidance. Specifically, the terms "financial purposes" and "readily available" are not defined, which would create significant confusion for market participants. Stretched to its logical conclusion, the Bureau's interpretation of "funds" could include any digital asset with even minimal market demand, even if the asset does not have a "financial purpose." This point is best illustrated using NFTs as an example.

NFTs are unique digital identifiers that are recorded using distributed ledger technology and may be used to certify authenticity and ownership of an associated right or asset. Each NFT has a unique token ID and almost always links to a URL that contains NFT metadata. That metadata may also include one or more URLs to a digital file, such as an image. If the NFT links to an image, it is usually the "face" of the NFT when it is displayed by applications that assist users to explore NFTs. As the NFT "lives" on a blockchain, its provenance and history are recorded, and if the blockchain is a public blockchain, this information is transparent to the public. The potential categories and use cases for NFTs are endless, much like a blank piece of paper carries almost infinite possibilities. The following categories are common examples of NFTs: digital art, trading cards, music records, redeemables, identity credentials, and many others.

Without clarity on what constitutes being "readily available for financial purposes," market participants could struggle to draw the line between NFTs that fall within scope and those that do not. The difficulty with the term is that it can fairly be understood as either requiring an asset to have a conceivable financial use, or to be truly financial in nature, i.e., representing a stock, bond, or other financial contract. We believe that the latter category will result in better regulatory outcomes and is correct as a substantive matter. The reality is that the majority of NFTs do not have a financial purpose and are purchased for personal consumption; for example, a user might purchase digital art.¹² While it is possible that purchasers could use digital art in a financial way, in the same manner that purchasers sometimes use physical art in that manner, that is not the primary design. The mere fact that digital art utilizes blockchain technology does not change its economic use case, and it would make little sense to treat it as a financial instrument on that basis alone. Moreover, if the Bureau were to base the status of an NFT on how its purchasers act, rather than the primary purpose of the NFT, the outcome would be highly unpredictable and non-administrable. In contrast, a small group of NFTs represent ownership over true financial assets or instruments, and this group could potentially be used for payment purposes (like currency) if they are redeemable for or serve as a store of value or medium of exchange. While there are not many active use cases for NFTs that fall into the financial

¹² We note that the value of these NFTs is unknown unless and until they are sold; NFTs are unique, non-fungible assets for which there is generally no readily determinable market price. This is unlike most fungible digital assets, like bitcoin and ether, which are traded in highly liquid markets and have a readily knowable price at any point in time. Therefore, it may also be unclear which NFTs have "monetary value."

instruments and payments category, treating only this category of NFTs as “funds” would result in clear and predictable outcomes. However, for the majority of NFTs that are in the consumption category, the Proposed Rule should not apply.

We also request clarification on whether NFT transactions would be exempt from the definition of “consumer payment transaction” in exchanges of NFTs for other NFTs, or when NFTs are exchanged for fungible digital assets and vice versa.¹³ NFTs are digital assets that can be and frequently are purchased with other digital assets, generally the native token of the blockchain network on which the NFT is deployed. Given this form of purchase, it would be helpful if the Bureau clarified this exemption in future iterations of the Proposed Rule.

B. Self-hosted digital asset wallets

The Proposed Rule does not take an explicit position on whether self-hosted wallet applications fall within its scope, but it states that a product or service provides “wallet functionality” if it (1) stores account or payment credentials, including in encrypted or tokenized form; and (2) transmits, routes, or otherwise processes such stored account or payment credentials to facilitate a consumer payment transaction. Based on this two-part test, we believe that self-hosted wallets fall outside the scope of the Proposed Rule, and we suggest that the Bureau adopt this position in future iterations of the Proposed Rule to avoid potential market confusion on this point.

A self-hosted wallet is a software or hardware tool that enables a user to interact with blockchain networks without relying on a third-party service. Consumers use self-hosted wallets to store information related to their digital assets, such as private keys that allow them to access, control, and transact with their digital asset holdings on blockchains, and public keys that are used as addresses to receive digital assets. Much like web users use web browsers to access the Internet, self-hosted wallets offer individuals a convenient way to maintain control over a blockchain address and retain any assets belonging to such an address, so that when desired they can easily interact with blockchain networks and others in a peer-to-peer manner. Self-hosted wallets can take the form of hardware wallets that store data in an encrypted format on a physical device, or software wallets that fulfill the same function on a consumer’s computer or mobile device. Perhaps most importantly, with a self-hosted wallet, the consumer holds all authorizing credentials, and that information is not visible to or hosted by a platform or third-party service provider without the consent of the consumer. In contrast, hosted wallets (also known as custodial wallets) function much like a traditional bank account where a third party retains responsibility over personal information and the assets associated with an address.

Self-hosted wallets should not fall within the scope of the Proposed Rule because these wallets are not directly involved in the execution of consumer transactions. While it is true that certain self-hosted wallets could fall within the first prong of the “wallet functionality” test if the wallet offers near field communication capabilities or generates QR codes for consumers to

¹³ See Proposed Rule, 1090.109(a)(2)(B)(1) (exempting from the definition of “consumer payment transaction” a transfer of funds “(1) that is linked to the consumer’s receipt of a different form of funds” including a crypto-for-crypto transaction).

initiate transactions with merchants at point-of-sale terminals, self-hosted wallets fall outside the second prong of the Proposed Rule. Self-hosted wallets have no role in transmitting, routing, or processing transactions or payment credentials that are executed using the wallet; the wallet is a tool that enables users to interact with blockchain networks by allowing them to sign and broadcast cryptographic messages to blockchains. Indeed, the primary role of self-hosted wallet providers is to offer the software or hardware for consumers to store their private keys and manage their own digital asset holdings in a convenient manner, and providers have no visibility into a wallet's payment credentials and the transactions that users conduct (other than information that is publicly available to anyone on the blockchain ledger).¹⁴ It is the blockchain network itself that autonomously facilitates and self-executes the actual transmission of digital assets between wallets and records transfers of ownership. There is no payment processor or other similar intermediary as there would be for a traditional payment transaction. A self-hosted wallet is analogous to a physical billfold where one might retain identification cards or dollar bills or a home self-deposit box where one retains a title to a valuable asset. The Proposed Rule should not capture self-hosted wallets. In future iterations of the Proposed Rule, we encourage the Bureau to acknowledge the distinct features of self-hosted wallets and clarify that they are outside the scope of the Proposed Rule.

III. Requested Modifications to Proposed Rule

We urge the Bureau to more narrowly define the market it seeks to supervise to expressly exclude providers that support certain types of digital asset transactions. In particular, the Bureau should consider:

- Adding preamble language or additional verbiage to the definition of “consumer payment transaction” to clarify that the Proposed Rule does not cover all digital assets.
- Further defining and carefully clarifying, after true coordination with the CFTC and SEC, characteristics which make certain digital assets “readily usable for financial purposes” so as not to give different treatment to similarly situated or classified commodities or securities.
- Taking the position that the definition of “wallet functionality” does not include self-hosted wallets that merely broadcast consumer payment transaction information to the blockchain network and are not otherwise involved in transaction routing.
- Clarifying that certain blockchain technologies are outside the scope of the Proposed Rule as described in Footnote 6.

We believe that these modifications would provide a heightened measure of clarity and predictability to the digital assets industry before the Bureau formalizes its supervisory authority in the market.

¹⁴ See 12 U.S.C. § 5481(11) (excluding from the Bureau's jurisdiction “electronic conduit services” or “the provision, by a person, of electronic data transmission, routing, intermediate or transient storage, or connections to a telecommunications system or network . . . ”)

IV. Conclusion

A16z is grateful for the opportunity to comment on the Proposed Rule. While we share the Bureau's recognition of the importance of this market, we urge the Bureau to thoughtfully consider the points we raise. Please do not hesitate to reach out if you have any questions regarding this letter, or if you would like to discuss further.

Respectfully submitted,

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