

Crypto-assets regulation in the EU

On 5 October 2022, the European Council approved its position on the Markets in Crypto Assets (MiCA) regulation. It has been a long process of negotiations and amendments since the first proposal was presented by the European Commission in September 2020. On 10 October 2022, the Committee on Economic and Monetary Affairs voted to confirm the proposal for the MiCA regulation. The regulation is not officially adopted, however, as it awaits a vote from the larger European Parliament plenary. When adopted, we expect the regulation to take effect from the second half of 2024.

Introduction

The MiCA regulation is the first of its kind in the world that will apply to crypto-assets, crypto-assets issuers and crypto-assets service providers (CASPs) across all EU member states, including EEA members. The aim of the regulation is to provide clarity to companies, customers, regulators and other stakeholders that are involved in the offering/purchasing/regulating of crypto-asset related services and products. In addition, the regulation aims to ensure financial stability in markets, and protect both consumers and professional investors from various risks.

What is the difference between previous drafts and the final version?

One of the main discussion points in previous iterations of MiCA regulation was regarding the scope of the regulation, e.g. on whether or not to include a framework for Non-Fungible Tokens (NFTs), Decentral Finance (DeFi), Decentralized Autonomous Organizations (DAOs) and Proof of Work mining activity (PoW). In brief, NFTs, DeFi, DAOs and PoW are currently not covered in this proposed version of MiCA. However, we would like to stress that with regards to these topics there are some important elements to be considered and exemptions in the current text.

NFTs, are as mentioned, not included. However, fractionalized NFTs will be treated like utility tokens and issuers will have to register with authorities and present a whitepaper and other requirements listed. This opens up room for interpretation and possible attempts to exploit work arounds to the MiCA regulation. In addition, one should also keep in mind the fact that even if NFTs in general are not covered, this does not mean that they could not be qualified as a financial instrument. Hence, a case by case interpretation of the attributes of the token will be necessary in order to determine if it is covered by MiCA or not, or whether there are other applicable financial market rules and requirements which need to be applied.

Similarly, DeFi and DAOs are not covered by MiCA, as long as the services are provided in a fully decentralized manner – i.e. without any intermediary. However, there are ongoing discussions at EU level as to the creation of

a separate regulatory framework specifically aimed at DeFi, DAOs etc. as well. It would be therefore prudent, not to expect these areas to be a “free haven” where no laws or taxes are applicable. Neither now, nor in the future.

With regards to PoW mining activity, there are no direct ban as previous versions of MiCA had proposed. However, there is a clause in the final draft relating to environmental impact that requires market participants covered by MiCA to disclose information about their environmental and climate footprint. This should be seen in the context of significantly energy consuming mining activity. The European Securities Markets Authority (ESMA), with the assistance of the European Banking Authority (EBA), will be tasked with the drafting of technical standards on the content, methodologies and presentation of information related to climate and other environment adverse impacts.

As established in previous drafts, MiCA defines three types of tokens. Utility Tokens, Asset reference Tokens (ARTs) and E-money Tokens (EMTs). A Utility Token is essentially all tokens that are not ART or EMT – e.g. Bitcoin, Ether, Mana etc.

ARTs are any crypto assets that derive its value from a basket of assets – e.g. stablecoins such as USDC, DAI etc. that are collateralized by cryptocurrencies. ART issuers do not have to register with any authorities as long as the market cap does not exceed EUR 5 million. If the threshold is exceeded, the issuer must maintain high quality reserves and will not be allowed to offer a yield. This means that issuers of ARTs shall ensure efficient and sound management of the reserve of assets in a way that issuance and redemption of these tokens are always matched by a corresponding increase or decrease of the reserve of assets. National competent authorities can if needed withdraw authorization of issuers of ARTs if the European Central Bank (ECB) or other central banks issue an opinion that the ARTs pose a serious threat to monetary policy, sovereignty or operation of payment systems.

EMTs fall within the category of centralized stablecoins – e.g. Tether, USDC etc. that are backed by fiat money. Rules applicable to EMTs will more or less be the same as for ARTs. However, stablecoins considered significant would have its transaction volumes capped at EUR 200 million per day.

Other relevant clauses in MiCA

► Custody responsibility

CASPs that provide custody services will be responsible and have to put mechanisms in place in order to protect consumers wallets. CASPs will be liable in case of loss of investors assets, unless they can prove that the loss has been caused by an external event out of reasonable control.

► Insider trading

MiCA will include elements to prevent insider trading, unlawful disclosure of inside information, market manipulation etc. with regards to crypto assets.

► Loyalty tokens

Loyalty tokens that cannot be transferred are excluded from the scope.

► Public register

ESMA will operate and maintain a public register of non-compliant entities for all member states. In addition, EBA will also oversee the crypto markets.

► Customer protection

In view of the lack of harmonized EU consumer protection rules MiCA introduces several provisions which CASPs and other stakeholders need to observe. Additionally, to ensure consumer protection, CASPs should comply with some prudential requirements.

► Supervision

As the supervision at EU level will involve, to different degrees, three different supervisors: ESMA, EBA and ECB. Hence, it will be important for firms to have a good understanding of what roles (and when) each of them plays.

ensure and verify the source of origin and parties involved. TFR is part of a larger package to strengthen anti-money laundering and countering terrorism financing (AML/CFT) rules which will become applicable when MiCA enters into force.

The TFR rules should also be seen in the context of Know Your Customer (KYC) guidance issued by Financial Action Task Force, which requires among others all DeFi developers to have KYC on all their users on its Decentralized platform.

Further, the OECDs Crypto Asset Reporting Framework (CARF) rules should also possibly be taken into consideration. The rules are expected to be published on October 10th 2022. This framework is a new global tax transparency framework with regards to the development of automatic information exchange on crypto assets. CARF will require e.g. crypto exchanges and wallet providers to apply procedures to identify their customers and to report customers transfers to tax authorities.

In brief, all of the above means that businesses involved in crypto asset products or services should prepare themselves to assess the impact of MiCA to their business, identify potential gaps and start early with implementation.

HVG Law has provided legal advice within this landscape since 2015, and HVG Law together with EY are happy to assist you with legal, strategic, business, legal, regulatory, compliance and tax challenges as well as opportunities that may arise from the world of cryptocurrencies.

Other regulation and guidance that should be seen in the context of MiCA

MiCA should be seen in the context of several other stakeholder initiatives, such as the EU Transfer of Funds Regulation (TFR) that sets out a framework for the so-called "Travel Rule", which means that all crypto transfers will be subject to extensive compliance rules to



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What HVG Law can do for you

We advise on all matters related to the blockchain space. From advising on and setting up Decentralized Autonomous Organizations (DAO), to advising on the applicable financial regulatory framework and from assisting with the registration of crypto-assets service providers with DNB to advising on the issuance of (security) tokens, NFTs and other cryptocurrencies.

As our track record in this space dates back to 2015, and we typically work in close collaboration with EY Tax on blockchain matters, HVG Law is ideally positioned to assist market parties in the blockchain space.

About HVG Law

HVG Law LLP (HVG Law) ranks amongst the top Dutch law firms and is characterized by an entrepreneurial, innovative and solution-driven approach. With more than 150 dedicated and pragmatic lawyers, including (candidate) Civil Law Notaries, HVG Law offers high-quality, legal services in a broad and multidisciplinary context. Our lawyers are active in all legal areas and sectors relevant to business, directors, shareholders and government authorities and have knowledge of your business and your market. At our offices in Amsterdam, Rotterdam, Utrecht, Eindhoven, New York, Chicago and San Jose (i.e., Donahue & Partners LLP in the USA), we are able to offer our legal services to national and international clients.

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