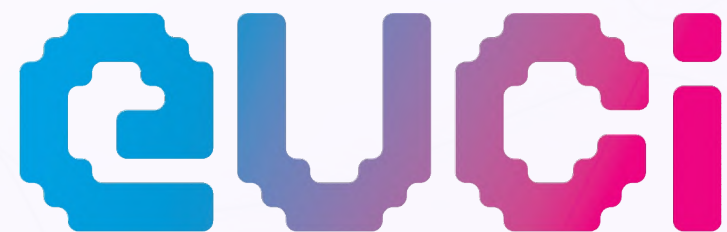


Pioneering the Unknown: MiCA's Open Enigmas in the EU and Beyond

Anja Blaj

February 2024



European Crypto Initiative

Hello!



European Crypto Initiative

We focus on regulatory frameworks aimed at addressing various challenges and risks associated with the crypto industry, such as investor protection, data privacy, and money laundering. We keep an eye on those rules they are likely to have a significant impact on the future development of the industry and will require careful consideration and analysis by all stakeholders involved.

Quick Overview:

I. Why MiCA?

II. Leaked drafts of MiCA Regulation

III. EU Legislative Process

IV. MiCA Regulation - Scope & Timeline

V. MiCA Exclusions

VI. Recent ESMA's Guidelines under MiCA

Why MiCA?

A blurred image of the Libra logo, which consists of three wavy lines followed by the word "libra" in a lowercase, sans-serif font.

MiCA's Significance Regime for Stablecoins - A Sledgehammer to Crack a Nut?

38 Pages • Posted: 7 Feb 2024

[Patrick Hansen](#)

Circle Internet Financial

[Helmut Bauer](#)

Flawless Money

Date Written: January 18, 2024

1. Introduction

It's all Libra's fault

Any analysis of the new EU rules for “significant” stablecoins inevitably needs to start with Facebook’s Libra project. Facebook published its Libra white paper in June 2019, which sparked a wave of hostile political reactions and instant discussions on financial stability, monetary sovereignty, and financial stability risks of stablecoins “with the potential for global reach”.

In October 2019, the G7 published their report “investigating the impact of global stablecoins”³, introducing the concept of “global stablecoins” or GSCs that could have significant adverse effects, both domestically and internationally, on the transmission of monetary policy, financial stability, efforts to combat money laundering and terrorist financing, and fair competition and antitrust policy.

Leaked first drafts of MiCA

Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (Text with EEA relevance)

2020/0265(COD)

DRAFT [Version after TM 20 September 2022]

20-09-2022 at 21h05



	Commission Proposal	EP Mandate	Council Mandate	Draft Agreement
Formula				
1	2020/0265 (COD)	2020/0265 (COD)	2020/0265 (COD)	2020/0265 (COD) <small>Text Origin: Council Mandate</small>
Proposal Title				
2	Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (Text with EEA relevance)	Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (Text with EEA relevance)	Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (Text with EEA relevance)	Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (Text with EEA relevance)

Who can propose new regulations in EU?

The EU's legislative process includes several key institutions: the European Commission, the European Parliament, and the Council of the European Union. Together, they work to create legislation that applies across all EU member states.

The European Commission	European Parliament	The Council of the EU
Has a right of legislative initiative - presents proposals for EU legal acts, either on its own or upon request from other EU institutions or in response to a citizens' initiative.	Legislators. May request the Commission to carry out studies and submit any appropriate legislative proposals.	

Treaty on the Functioning of the European Union identifies specific circumstances where the European Central Bank, the Court of Justice, and a quarter of the Member States (European Citizens' Initiative) also possess the right of initiative.

Who can participate in the regulatory process?

Data Act

[Open Letter](#)[Joint Statement](#)[About Data Act](#)[About Us](#)

Open Letter Summary

The letter advocates for technological neutrality, ensuring freedom of choice and adaptability of regulations, irrespective of the technology used. It also emphasizes the need for clarification within the Data Act, as the current text could inadvertently limit the use of Smart Contracts based on public/permissionless technology and introduce uncertainty for already deployed Smart Contracts. This scenario could pose significant challenges for SMEs who heavily rely on these Smart Contracts for their operations and business models.

While we understand the intention of the EU regulator was not to regulate smart contracts deployed on public/permissionless technology, our proposed refinements emphasize three key potential amendments that aim to clarify the regulator's intention and minimize potential negative impacts (in order of preference):

- 1. Substitute the term 'Smart Contract' with 'Digital Contract'** to reflect the Act's intended scope more accurately and to eliminate ambiguities about the applicability of Article 30's stringent requirements.
- 2. Clarify the scope of Article 30** in case the change of terminology proves unsuitable. In this scenario, we recommend revising Article 30 to narrow down its applicability to 'Smart Contracts' deployed on private and permissioned electronic data records.
- 3. Limit Article 2(16) to privately operated and permissioned electronic data records**, which, although it is the least favorable option, could still mitigate some of the potential negative impacts if the other two options do not materialize.

We believe these proposed changes align with the principle of technological neutrality, ensuring equal treatment to all technological solutions and fostering an environment conducive to innovation and growth.

Below you can read and download the Open Letter About Concerns and Proposed Refinements Regarding the Regulation of Smart Contracts in the Data Act. If you wish to support this Open Letter, send your logo and information about your organization's representatives to one of the organisations leading discussions about the Data Act. You can find our email addresses on the [About Us](#) page.

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European Crypto Initiative

POLICY

SUPPORTERS

TEAM

CONTACT



Propelling Europe
towards the future of
finance

The European Crypto Initiative aims to shape EU regulation to favour open, permissionless, decentralised applications leveraging blockchain technology while advocating for an innovative EU environment, supporting technological development for SMEs and innovative Crypto Assets Service Providers.

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Who can participate in the regulatory process?



MiCA: Scope and Timeline

1. The EU's overarching aim with MiCA is to create a “**risk-based regime**” that balances **consumer and investor protection, financial stability and monetary sovereignty concerns** whilst **accompanying innovation and ensuring EU competitiveness**.

2. **Material & subject scope** – MiCA applies to entities engaged in **crypto-assets issuance**, including **stablecoins (ARTs and EMTs)** and **services related to crypto-assets in the EU**. However, it does not cover crypto-assets qualifying as **financial instruments under MiFID (Markets in Financial Instruments Directive)** regardless of the technology used for their issuance - ESMA will clarify this classification.



MiCA: Issuing Crypto-Assets

Rules for issuing crypto-assets (other than stablecoins)

Rules for issuing crypto-assets largely follow those in **traditional securities offerings**.

To give a few examples, these are the regulated aspect of crypto-asset issuance:

- disclosure/transparency requirements through the issuance of a crypto-asset “**whitepaper**” (the equivalent of a prospectus),
- **marketing communications,**
- **professional behaviour,**
- **security,**
- **and managing conflicts of interests.**
- In addition, these digital assets will be supervised at a **national level**.

MiCA: Regulating Stablecoins

1. reference any value, right or a combination thereof **Asset Referenced Token (ARTs)** and
2. stablecoins that reference a single official currency **E-Money Tokens (EMTs)**.

ARTs and EMTs face significant additional rules on prudential and own-fund requirements, managing/investing their reserve of assets and redemption rights. They are also prohibited from granting interest and must have in place a recovery and redemption plan in the case of insolvency or any other difficult scenario.

Strict limitation when stablecoins are “widely used as means of exchange”:


- This limitation would apply to all ARTs and EMTs referencing a foreign currency if a threshold of €200 million in terms of **volume of payment transaction/day** and 1 million in terms of number of transactions (on a quarterly average) is met.
- Should that be the case, the issuer would have to either stop issuing the ART or present a 40 day plan to keep the issuance below the aforementioned thresholds.


MiCA Exclusions: DeFi & NFTs


- NFTs are generally excluded from MiCA's scope.
- **Fractioned parts** of a unique and non-fungible crypto-asset should not be considered unique and non-fungible.
- **Indicators of fungibility**, such as NFTs issued in large series/collections and regardless of the attribution of a unique identifier.
- **DeFi** is generally excluded by way of **Recital 22**: "Where crypto-asset services are provided in a fully decentralised manner without any intermediary, they should not fall within the scope of this Regulation."

Level 2 (and 3) measures?

MiCA is only the beginning of the work. Now it's time for the Level 2 (and 3) measures

 Before the time of MiCA's application date, different EU institutions (such as ESMA and EBA) will issue documents - regulatory technical standards, technical papers, (non-binding) opinions, etc. - that will further clarify some of the responsibilities under MiCA: examples include reserves, single currency area, CASPs reporting obligations, responsible persons.

 ESMA is also responsible for organising a dedicated crypto-asset task force - with the intention of, among other actions, discussing real cases brought by National Competent Authorities, market and regulatory developments, and common approaches and practices. The task force has been running since **March 2022**.

 The National Competent Authorities on a member-state level are key for implementing both MiCA and the DLT Pilot Regime. Therefore we all need to work closely with them.

Recent ESMA's Consultation Papers

- On the draft guidelines on reverse solicitation under MiCA
- On the draft Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

Reverse solicitation

- Reverse solicitation is defined as a situation where a client initiates, at their own exclusive initiative, the provision of services by a service provider
- It outlines the circumstances under which service providers can engage with clients without having to fully comply with the regulatory requirements typically imposed on solicitation activities
- Protect consumers by ensuring that any engagement is genuinely initiated by the client, rather than being the result of active marketing or solicitation by the provider

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

*Under Article 61(3) of MiCA, ESMA is mandated to issue guidelines: i) to **specify the situations** in which a third-country firm is deemed to solicit clients established or situated in the EU as well as ii) on **supervision practices** to detect and prevent circumvention of the reverse solicitation exemption.*

Annex II of Consultation paper includes guidelines, which set criteria defining reverse solicitation, outline responsibilities of third-country firms towards clients within EU, and propose methods for ensuring compliance and monitoring.

 [See the original document here.](#)

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

Notably the paper:

- provides detailed guidance on the solicitation of customers by third-country companies, including the methods of solicitation, the person soliciting, the sole initiative of the customer, and when a cryptocurrency service is of the same type as another.
- addresses control practices to detect and prevent circumvention of the reverse solicitation exception.
- they emphasize monitoring, exchanges with other authorities and responding to customer complaints or "whistleblowers".

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

Types of Cryptoassets under Article 61 of MiCA

- Crypto-assets belong to the same type if they have same features, rights, and obligations
- The distinction could involve variations in the underlying technology, the rights conferred by the crypto-asset (such as voting rights or entitlement to dividends), the asset's purpose (e.g., utility vs. security tokens), or the economic function and use case of the asset
- Ensuring that classifications reflect the asset's characteristics, preventing the bundling of fundamentally different assets under a single regulatory umbrella

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

Obligations of third country service providers

Must comply with specific obligations to offer services within the EU, including:

- adhere to MiCA's regulatory framework,
- ensure fair competition,
- maintain market integrity,
- establish a legal presence in the EU,
- provide clear information about their services, and ensure consumer protection.

Promoting transparency and safeguarding against potential risks associated with cross-border activities.

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

QUESTIONS

- Q1: Do you agree with the approach chosen by ESMA? Do you see any potential loophole that could be exploited by third-country firms to circumvent the MiCA authorisation requirements?
- Q2: Are you able to provide further examples of pairs of crypto-assets that would not belong to the same type of crypto-assets for the purposes of Article 61 of MiCA? Or are you able to provide other criteria to be taken into account to determine whether two crypto-assets belong to the same type
- Q3: Do you consider the proposed supervision practices effective with respect to detecting undue solicitations? Would you have other suggestions?

ESMA's Consultation Paper on the draft guidelines on reverse solicitation under MiCA

OPINIONS

- Reverse solicitation rules should apply for **AMLR** and **TFR** similarly to the application re MiCA.
- Prohibition **should not apply** to validators, personal (self-custodial) wallets, non-custodial smart contracts (such as DeFi protocols), non-custodial bridges because none of them is a CASP.

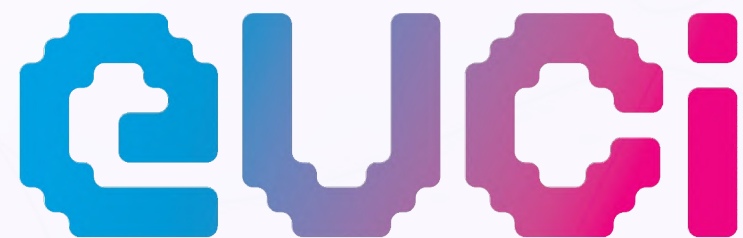
ESMA's Consultation Paper on the draft Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments

- **Transferable securities classification:** encompassing a variety of instruments considered as financial instruments, with specifics laid out in MiFID II.
- **Other financial instruments classification:** including money-market instruments, units in collective investment undertakings, derivatives, and emission allowances, each with unique characteristics and regulatory considerations.
- **MiCA's Crypto-Asset categorization:** outlining utility tokens, NFTs, and hybrid tokens, offering a framework for understanding the regulatory approach to different types of crypto-assets

ESMA's Consultation Paper on the draft Guidelines on the conditions and criteria for the qualification of crypto-assets as financial instruments

- There is no commonly adopted application of the definition of 'financial instrument' under MiFID in the EU.
- ESMA is not expected to clarify the entire scope of what constitutes a financial instrument, but only products that comply with both the crypto-asset definition of MiCA and the financial instrument definition of MiFID II
- Offerors or persons seeking admission to trading of crypto-assets are primarily responsible for the correct classification of such assets. This classification might, however, be challenged by the relevant NCA, both before the date of publication of the offer and at any time thereafter

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Pitch

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