

MiCA: the new EU cryptoasset law

The European Commission has been working on a comprehensive legislative and regulatory framework for all cryptoassets since 2019. One of the outcomes from this work is the proposed **Markets in Crypto-assets Regulation (MiCA)** which is expected to be published in September 2020. From the draft seen by XReg, it is clear that its scope is extensive and that its effect will be profound, not only in the European Economic Area (EU plus Iceland, Liechtenstein and Norway) but throughout the world. No stone has been left unturned. All cryptoassets and cryptoasset activities will be caught by the new legislation when it comes into force, including existing coins and tokens. MiCA aims to bring much-needed legal and regulatory certainty, to support innovation, to provide consumer and investor protection, and to ensure financial stability. As an EU Regulation, it will be directly applicable throughout the EEA without the need for national legislation.

MiCA will undoubtedly shake up the industry and have a profound impact on all cryptoasset activities and issuers in the EEA and the world.

The draft proposed Markets in Crypto-assets Regulation:

- seeks to bring into scope everything that is *a digital representation of value or rights, which may be transferred or stored electronically, using distributed ledger or similar technology*. Cryptoassets that fall within the definitions of financial instruments or electronic money under the existing Markets in Financial Instruments Directive and the Electronic Money Directive are excluded from MiCA. Where they already exist, MiCA will replace national frameworks for cryptoassets that are not covered by existing EU financial services legislation.
- sets out specific rules for stablecoins, which are defined as either *asset-referenced tokens* or *e-money tokens*. Additional rules will apply to those asset-referenced and e-money tokens that are deemed *significant*.
- will apply to a broadly defined group of *crypto-asset service providers* (CASPs) and *issuers* of cryptoassets (essentially anyone who offers cryptoassets to third parties), with more specific rules for issuers of asset-referenced tokens and e-money tokens.
- will implement transparency and disclosure requirements, establish consumer protection rules, introduce minimum capital requirements, as well as measures to prevent market abuse and ensure the integrity of cryptoasset markets. Although the regulations do not directly address anti-money laundering and terrorist financing risks, they are designed to further harmonise EU legislation with the Financial Action Task Force's Recommendations through the alignment of terminology and scope of services.

Will the requirement to incorporate a legal entity disrupt DeFi?

Among the many regulatory obligations that will be imposed on EU cryptoasset issuers and service providers is the need to be incorporated as a legal entity and for service providers to have their registered office in a Member State. One of the fastest evolving and most significant trends in the cryptoasset industry today is decentralised finance or *DeFi*. There can be little doubt MiCA will present significant challenges for those involved in DeFi projects.

Although intended to level the playing field, MiCA may be tilted, unintentionally, towards traditional financial services incumbents.

Transitional arrangements will allow CASPs already operating in the EEA to continue doing so while they seek authorisation under the new regime. Financial institutions such as banks, investment firms, and payment institutions will not need prior authorisation under MiCA in order to offer cryptoasset services.

Although the proposed regime aims to address proportionality and support innovation, only time will tell whether it does so effectively or if the regulatory burden will be too large for the smaller players to bear, stifling innovation and driving market consolidation.

MiCA will serve to harmonise cryptoasset regulation across the EEA and will replace any national legal and regulatory regimes for cryptoasset activities. An EEA-wide approach means that CASPs authorised in one Member State will gain access to the Single Market by passporting their services.

MiCA will not only affect cryptoasset service providers and issuers. Competent authorities across the EU will need to familiarise themselves with the new regulations to operationalise the regime and build capacity. This will require upskilling staff to be able to assess, evaluate, and understand the risks associated with cryptoassets and CASPs, and expanding their resources to safely authorise and supervise the sector.

CASPs as well as issuers of cryptoassets, e-money, and asset-referenced tokens currently operating in the EU will need to brace themselves for a wave of new regulatory obligations. This will be especially true for those currently operating in an unregulated environment. Boards and senior management, including those of CASPs and issuers located in third countries that target the EU market, will need to make important strategic decisions that will dictate the future success of their business.

This note is based on the draft of the proposed MiCA Regulation circulating at the time of publication, a copy of which XReg Consulting has obtained from a public source. It does not constitute legal or regulatory advice. **MiCA has profound implications for cryptoassets: payment, investment and utility tokens, stablecoins, crypto-asset service providers, and issuers.** XReg will continue to provide information and commentary as MiCA progresses into legislation and beyond.

If you would like to discuss MiCA or anything in this note, please email Ernest Lima at ernest@xreg.consulting.