

REGULATING GSCs – AND A FIRST VIEW ON MICAR

Prof. Dr. Dirk A. Zetsche, LL.M.
ADA Chair in Financial Law (inclusive finance)
University of Luxembourg

Regulating GSC

- I. The Issue
- II. International Perspective
- III. The Draft MICAR
- IV. Three Comments
- V. Conclusion & Take Away

I. The Issue

A. From Intermediary- to Platform-based Payments

B. Libra as Catalyst

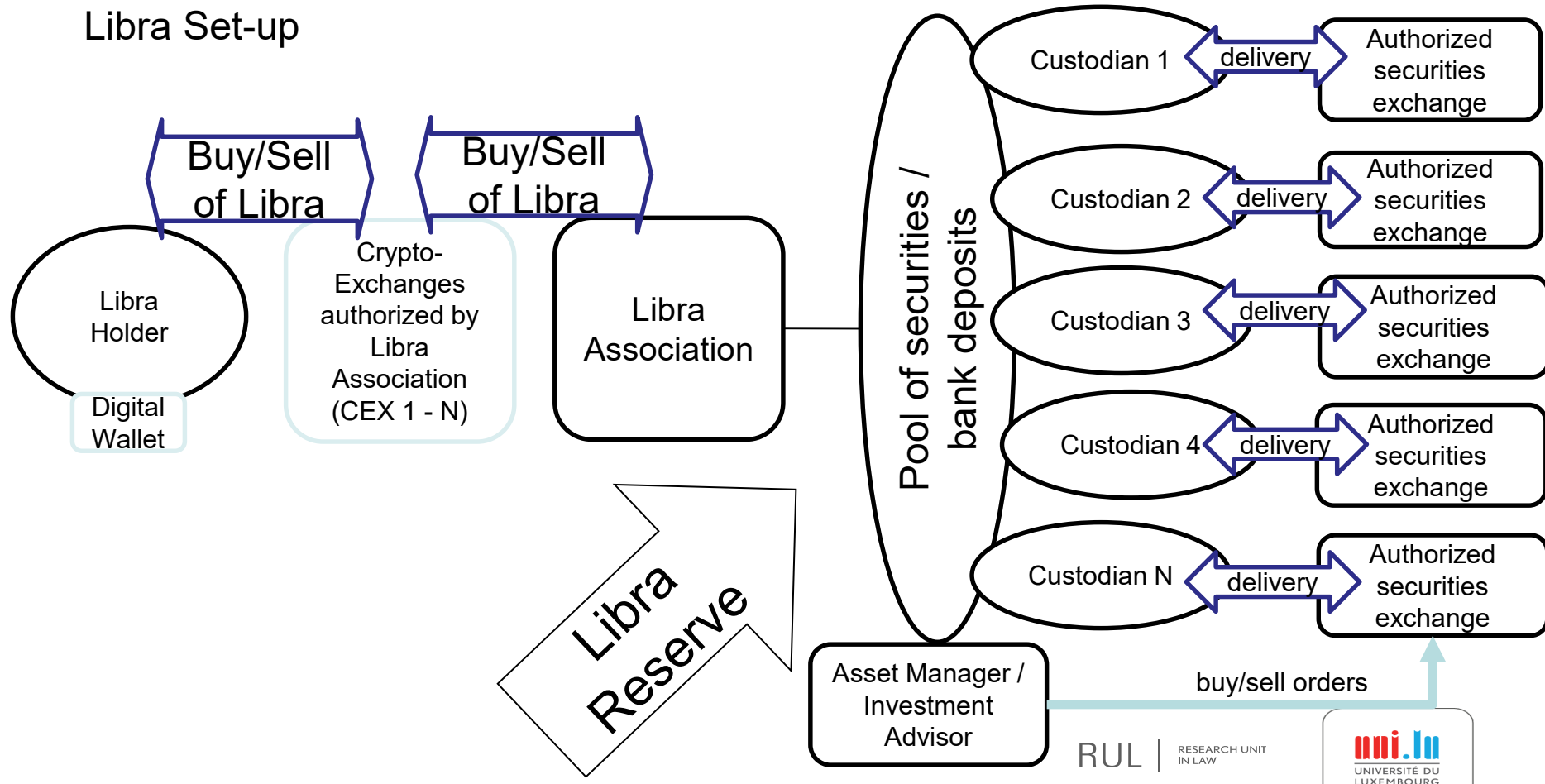
1. Technology
2. Funding
3. Size in terms of customers

C. About Gaps and Uncertain Scope of Regulation

Regulating Libra
www.ssrn.com/abstract=3414401

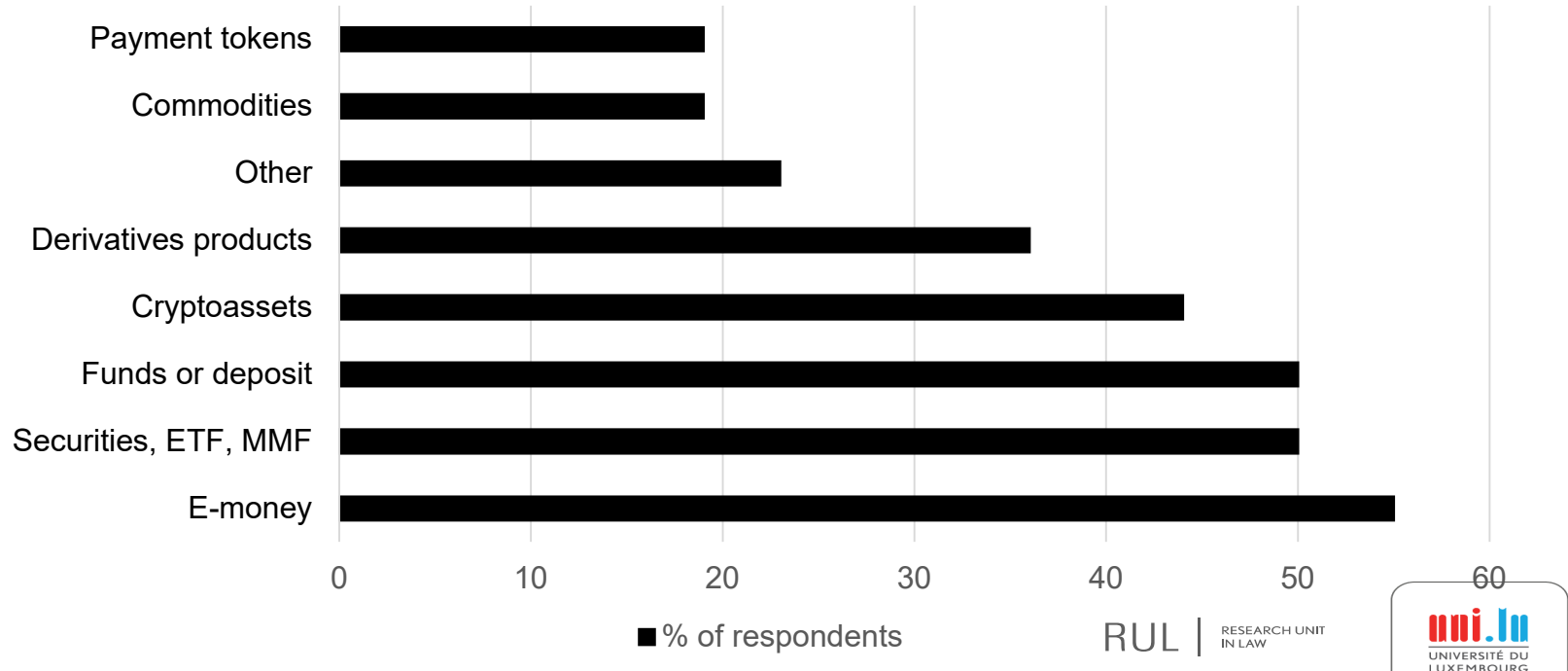


Libra Set-up



Survey among NCAs on regulatory, oversight and supervisory frameworks applicable to global stablecoins

Regulatory frameworks that could apply to stablecoins



I. The Issue

A. From Intermediary- to Platform-based Payments

B. Libra as Catalyst

1. Technology
2. Funding
3. Size in terms of customers

C. About Gaps and Uncertain Scope of Regulation

D. Regulatory Objective

1. Client Protection?
2. Systemic Risk?
3. Market Integrity?

II. International Perspective

□ FACULTY OF LAW, ECONOMICS AND FINANCE

- IOSCO Global Stablecoin Initiatives (March 2020)
- FSB Consultative Document on Global Stablecoins (April 2020): Financial Stability
- FATF Report to G20 on So-called Stablecoins (July 2020): Market Integrity



III. The Draft MiCAR

- A. EU Digital Finance Strategy
- B. A Primer to MiCAR – with a focus on GSCs
- C. Supervision of GSC under MiCAR

EU DIGITAL FINANCE STRATEGY of 24 Sept 2020



Plus
proposal for digital operational
resilience



Plus
Proposal to clarify or
amend certain related EU
financial services rules

*EU Com: Option 1 – bespoke legislative regime aimed at
addressing the risks posed by ‘stablecoins’ and ‘global
stablecoins’*

Brussels, 24.9.2020
COM(2020) 594 final

2020/0267 (COD)

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)

{SEC(2020) 306 final} - {SWD(2020) 380 final} - {SWD(2020) 381 final}

Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on a pilot regime for market infrastructures based on distributed ledger technology

(Text with EEA relevance)

{SEC(2020) 308 final} - {SWD(2020) 201 final} - {SWD(2020) 202 final}

B. MiCAR's ToC

Title I: Subject Matter, Scope and Definitions

Title II: Crypto-Assets, other than asset-referenced tokens or e-money tokens

Title III: Asset-referenced Tokens

Title IV: Electronic Money Tokens

Title V: Authorisation and operating conditions for Crypto-Asset Service providers

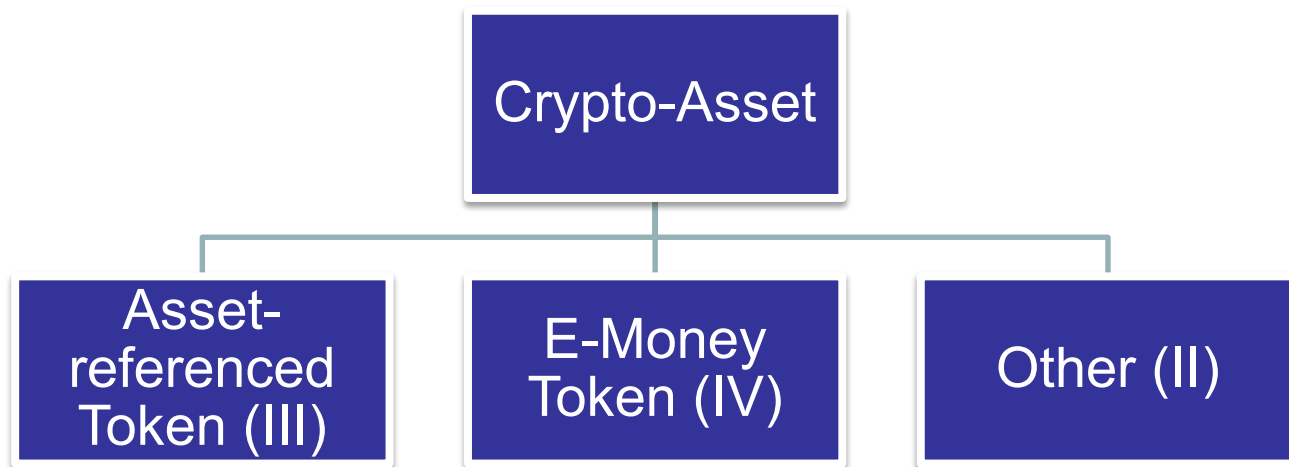
Title VI: Prevention of Market Abuse involving crypto-assets

Title VII: Competent Authorities, the EBA and the ESMA

Title VIII: Delegate Acts and Implementing Acts

Title IX: Transitional and Final Rules

Definitions



Definitions

Crypto Asset

'crypto-asset' means a digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology;

GSC

Asset-referenced Token (ART)

crypto-asset that purports to maintain a stable value by referring to the value of several fiat currencies that are legal tender, one or several commodities or one or several crypto-assets, or a combination of such assets;

E-money Token (EMT)

crypto-asset the main purpose of which is to be used as a means of exchange and that purports to maintain a stable value by referring to the value of a fiat currency that is legal tender;

Definitions

Asset-referenced tokens

- 'Global Stable Coin'

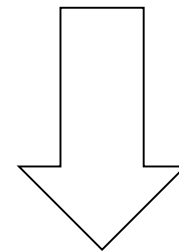
E-money tokens

- Payment tokens – 1:1: 'Stable Coins'

Other Crypto-assets

- Usage tokens

Security
Tokens?



EU Securities Law:
ProspectusR, MiFID,
Transparency
Directive

Title II: Crypto-Assets, other than asset-referenced tokens or e-money tokens

'Special Prospectus Regulation'

Article 4 Offers of crypto-assets (...) to the public, and admission of such crypto-assets to trading on a trading platform for crypto-assets

Article 5 Content and form of the crypto-asset white paper

Article 6 Marketing communications

Article 7 Notification of the crypto-asset white paper, and, where applicable, of the marketing communications

Article 8 Publication of the crypto-asset white paper, and, where applicable, of the marketing communications

Article 9 Offers to the public of crypto-assets (...) that are limited in time

Article 10 Permission to offer crypto-assets (...) to the public or to seek admission for trading such crypto-assets on a trading platform for crypto-assets

Article 11 Modification of published crypto-asset white papers and, where applicable, published marketing communications after their publication

Article 12 Right of withdrawal

Article 13 Obligations of issuers of crypto-assets (...)

Article 14 Liability of issuers of crypto-assets (...) for the information given in a crypto-asset white paper

Title III: Asset-referenced Tokens (GSC)

«issuance» of ART Regulated activity, subject to licensing

Chapter 1

Authorisation to offer asset-referenced tokens to the public and to seek their admission to trading on a trading platform for crypto-assets

Article 15 Authorisation

Article 16 Application for authorization

Article 17 Content and form of the crypto-asset white paper for asset-referenced tokens

Article 18 Assessment of the application for authorization

Article 19 Grant or refusal of the authorization

Article 20 Withdrawal of the authorization

Article 21 Modification of published crypto-asset white papers for asset-referenced tokens

Article 22 Liability of issuers of asset-referenced tokens for the information given in a crypto-asset white paper

Legal entity to be located in EU

Title III: Asset-referenced Tokens

Operating Conditions

Chapter 2

Obligations of all issuers of asset-referenced tokens

*Article 23 **Obligation to act honestly, fairly and professionally in the best interest of the holders of asset-referenced tokens***

*Article 24 **Publication of the crypto-asset white paper, and, where applicable, of the marketing communications***

*Article 25 **Marketing communications***

*Article 26 **Ongoing information to holders of asset-referenced tokens***

*Article 27 **Complaint handling procedure***

*Article 28 **Prevention, identification, management and disclosure of conflicts of interest***

*Article 29 **Information to competent authorities***

*Article 30 **Governance arrangements***

*Article 31 **Own funds requirements***

350 TEUR plus
2% of Reserve Assets
in Tier 1 Assets ('Equity')

Title III: Asset-referenced Tokens

CHAPTER 3 RESERVE OF ASSETS

*Article 32 **Obligation to have reserve assets, and composition and management of such reserve of assets***

*Article 33 **Custody of reserve assets***

*Article 34 **Investment of the reserve assets***

*Article 35 **Rights on issuers of asset-referenced tokens or on the reserve assets***

*Article 36 **Prohibition of interest***

Reserve Management:
Minimal market and credit
risk ('state funding')

Asset Segregation

Title III: Asset-referenced Tokens

CLEAR POLICY on Asset Holders rights (Art. 35 I)

Including

- (a) Conditions, including thresholds, periods and timeframes, to exercise those rights;
- (b) Redemption mechanisms and procedures, incl. under stress, insolvency etc;
- (c) Valuation of the asset-referenced tokens and of the reserve assets
- (d) Settlement conditions;
- (e) Fees.

Where rights are not granted to all token holders : Liquidity Management, but

=> **Statutory redemption right** if 'market value of asset-referenced tokens varies significantly from the value of the reference assets or the reserve assets' => Semi-open ended; requires designated market maker

No position on holders' rights:
« open » or « closed end »

Crypto-Asset Services and Authorized Activities

TITLE V: Authorisation and operating conditions for Crypto-Asset Service providers

Chapter 1: Authorisation of crypto-asset service providers

Article 53 *Authorisation*

1. Crypto-asset services shall only be provided by legal persons that have a **registered office in a Member State** of the Union and that have been **authorised as crypto-asset service providers** in accordance with Article 55

=> All token types subject to MiCAR.

‘crypto-asset service’ means **any of the services and activities listed below relating to any crypto-asset**:

- (a) the **custody** and administration of crypto-assets on behalf of third parties;
- (b) the operation of a **trading platform** for crypto-assets;
- (c) the **exchange of crypto-assets for fiat currency** that is legal tender;
- (d) the exchange of crypto-assets for other crypto-assets;
- (e) the execution of orders for crypto-assets on behalf of third parties;
- (f) placing of crypto-assets;
- (g) the reception and transmission of orders for crypto-assets on behalf of third parties
- (h) providing advice on crypto-assets;

C. Regulation of Significant ART Issuers [GSC]

Article 98 Supervisory responsibilities of EBA on issuers of significant asset-referenced tokens and issuers of significant e-money tokens

“Where an asset-referenced token has been classified as significant in accordance with Article 39 or Article 40, the issuer of such asset-referenced tokens shall carry out their activities under **the supervision of the EBA.**”

⇒ Direct supervisory powers. Details laid out in Articles 103 et seq.

EBA as competent authority
Banking Law concerns prevail =>
systemic risk?

Title III: Asset-referenced Tokens

CHAPTER 4

ACQUISITIONS OF ISSUERS OF ASSET-REFERENCED TOKENS

Article 37 Assessment of intended acquisitions of issuers of asset-referenced tokens

Article 38 Content of the assessment of intended acquisitions of issuers of asset-referenced tokens

CHAPTER 5

SIGNIFICANT ASSET-REFERENCED TOKENS

Article 39 Classification of asset-referenced tokens as significant

Article 40 Voluntary classification of asset-referenced tokens as significant

Article 41 Specific additional obligations for issuers of significant

Chapter 6

Orderly wind-down

Article 42 Orderly wind-down

Size & Market Integrity & Monetary Stability

EBA to classify

- (a) the size of the customer base, the shareholders of the issuer of asset-referenced tokens or of any of the third-party entities
- (b) the value of the asset-referenced tokens or market capitalisation;
- (c) number and value of transactions
- (d) the size of the reserve of assets
- (e) the significance of the cross-border activities
- (f) the interconnectedness with the financial system.

Title IV: Electronic Money Tokens

Chapter 1

Requirements to be fulfilled by all issuers of electronic money tokens

*Article 43 **Authorisation***

*Article 44 **Issuance and redeemability of electronic money tokens***

*Article 45 **Prohibition of interests***

*Article 46 **Content and form of the crypto-asset white paper for electronic money tokens***

*Article 47 **Liability of issuers of e-money tokens for the information given in a crypto-asset white paper***

*Article 48 **Marketing communications***

*Article 49 **Investment of funds received in exchange of e-money token issuers***

Chapter 2

Significant e-money tokens

*Article 50 **Classification of e-money tokens as significant e-money tokens***

*Article 51 **Voluntary classification of e-money tokens as significant e-money tokens***

*Article 52 **Specific additional obligations for issuers of significant e-money tokens***

Third Country Dimension

EBA-lead
supervisory colleges

Article 99 Colleges for issuers of significant asset-referenced tokens

1. Within 30 calendar days of a decision to classify an asset-referenced token as significant, the EBA shall establish, manage and chair a consultative supervisory college for each issuer of significant asset-referenced tokens to facilitate the exercise of its supervisory tasks under this Regulation.

2. The college shall consist of:

(a) the EBA, as the chair of the college;

(b) ESMA;

(c) the competent authority of the home Member State where the issuer of significant asset-referenced tokens is established

...

(i) the ECB; ...

(k) relevant supervisory authorities of third countries with which the EBA has concluded an administrative agreement in accordance with Article 108. => but no voting rights on non-binding opinions.

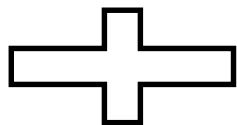
Article 108, 109 : Exchange of information with
authorities

No option to accept lead by
third country authority.

IV. Three Comments

1. Defining Crypto-Assets as a challenge
2. Precision, Consistency & System of European FL?
3. Interoperability MiCAR – Two-layered CBDCs?

1. Definition: Crypto-Asset



Digital bearer shares,
but 'Financial
instrument'

'crypto-asset' means a digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology;

Digital 'booking numbers' in a
bank account?
Position on credit card?

...

Definitional issues on
MS level will translate
into MiCAR scope
issues.



Title in DLT land registry? => title
is transferred by different means
than by the register position,
register follows

2. System of Law etc.

And / Or?
Documents: both

Small ART issuer exemption (Art. 15 (3) draft MiCAR)

No authorization for issuers of asset-referenced tokens if:

‘(a) over a period of 12 months, calculated at the end of each calendar day, the average outstanding amount of asset-referenced **tokens does not exceed EUR 5 000 000**, or the equivalent amount in another currency;

(b) the offer to the public of the asset-referenced tokens is **solely addressed to qualified investors** and the asset-referenced tokens can only be held by such qualified investors.

Issuers of such asset-referenced tokens shall, however, **produce a crypto-asset white paper** as referred to in Article 17 and notify that crypto-asset white paper, and where applicable, their marketing communications, to the competent authority of their home Member State in accordance with Article 7.’

Why WP for QI?
[≈Art. 23 AIFMD]

Why 5 Mio., not 8 Mio? [Art.3 II
lit. b PR]

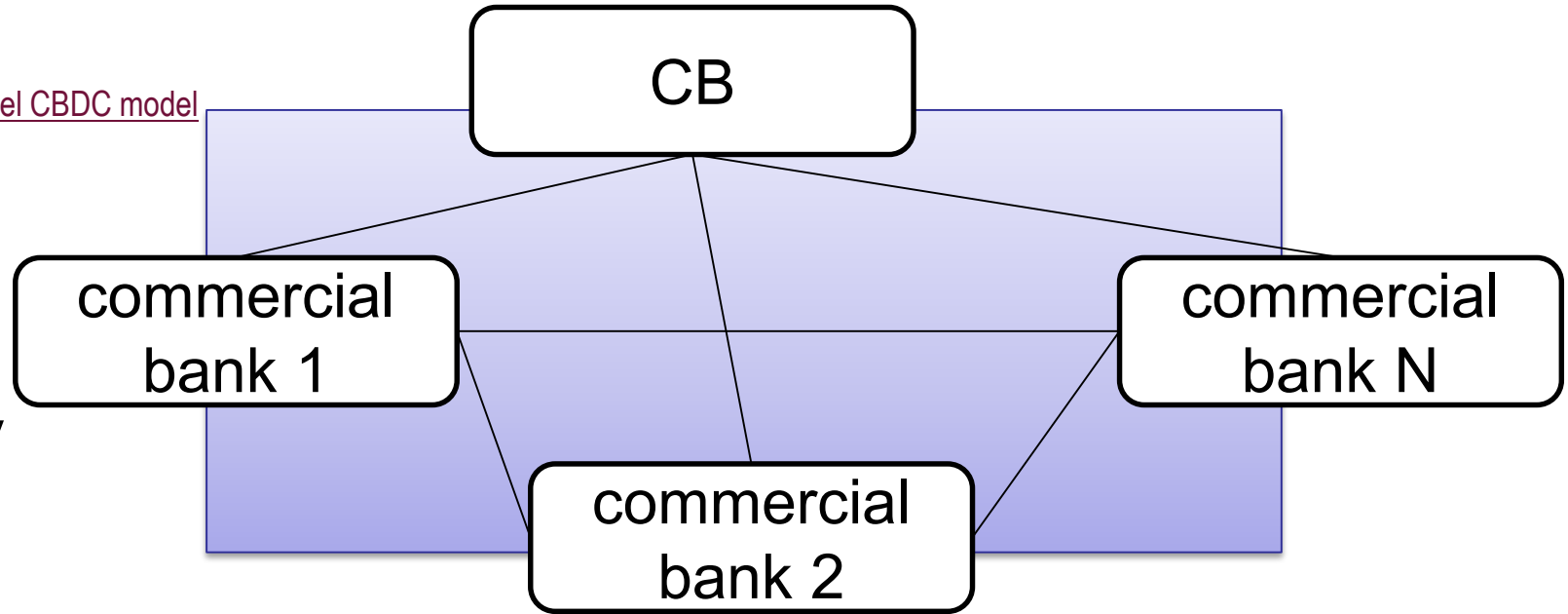
Financial Stability?
=> Significant ART,
not authorized?

3. MiCAR vs CBDCs

- Full exemption for CBDCs and Central Banks
- Uncertainty where CBDC services provided not « on behalf of Central Banks »

First level CBDC model

Trusted
Inter-
mediary



2nd level intermediaries (PSD, emoney, small banks)

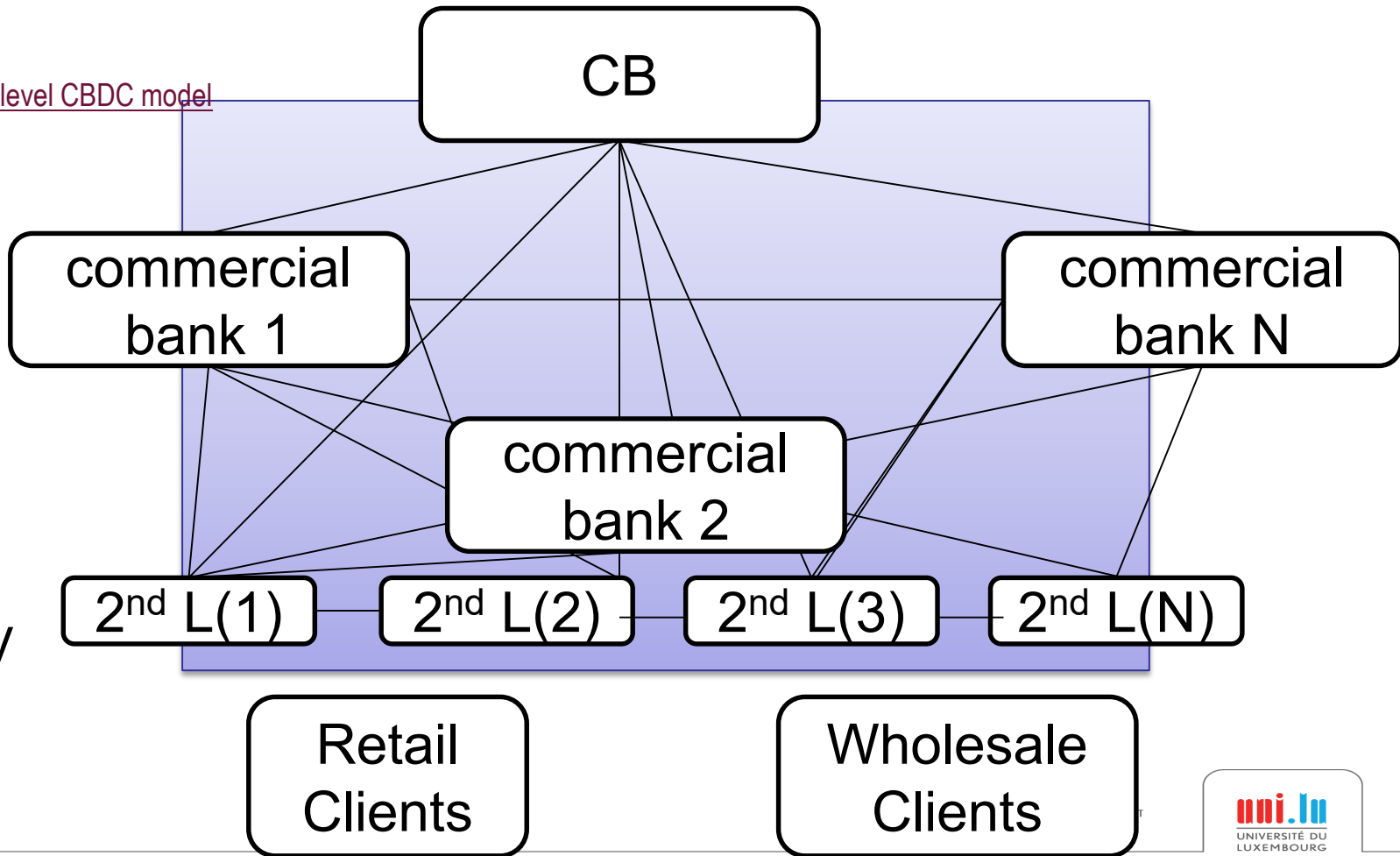
Retail
Clients

Wholesale
Clients

Second level CBDC model

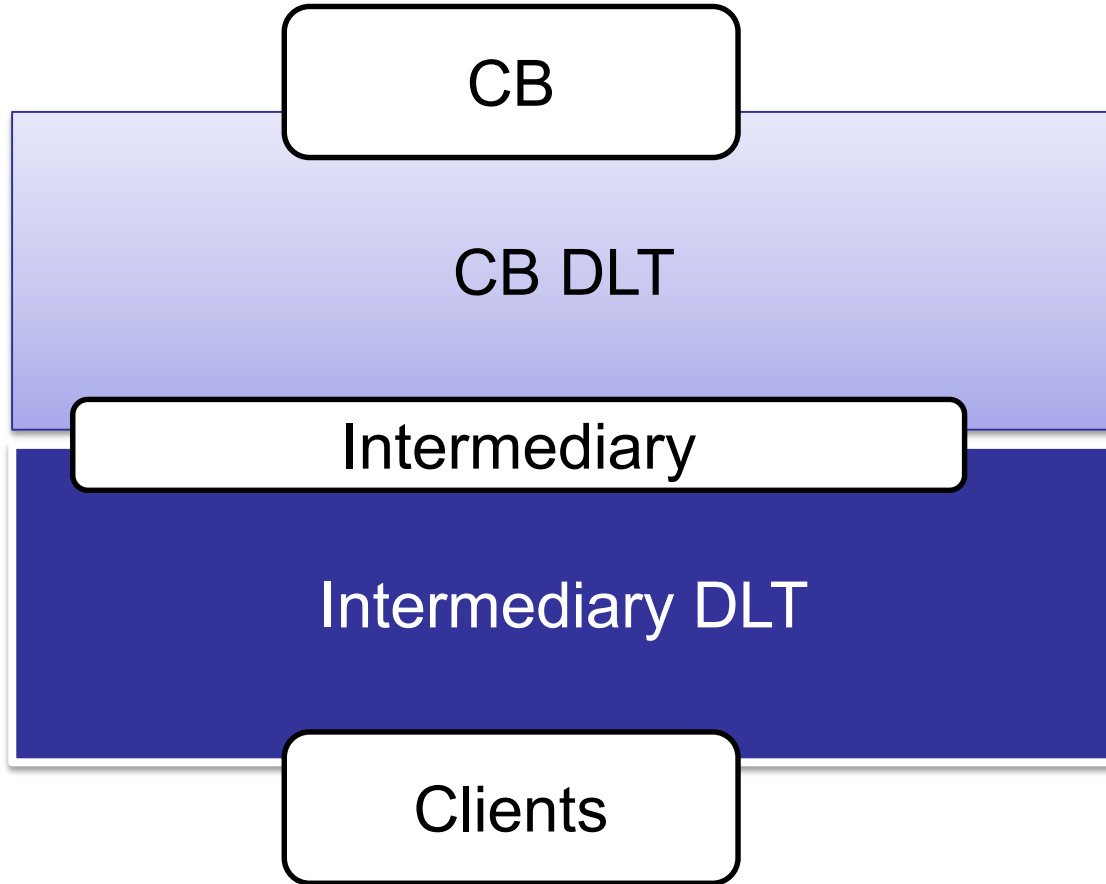
Trusted
Inter-
mediary

2nd Lvl
Inter-
mediary



Two layer CBDC model

**MiCAR
applies =>
Reserve
Assets etc.**



V. Conclusion & Takeaways

- Global Stablecoins made the need to regulate the Token economy too obvious to ignore.
- IOSCO, FSB, FATF as Macro Framework
- MiCAR as Micro Framework
 - MiCAR as Gap Filling Exercise: bespoke regulation for GSC
 - Issuers and Service Providers to be authorized and regulated
 - Leans on different familiar concepts: banking, fund, prospectus
 - Boundaries between MiCAR and general financial law uncertain; general financial law > MiCAR.
 - Cooperation with 3rd countries through colleges, but lead of EBA; no scheme to accept lead of 3rd country authority
 - Could create difficulties re certain CBDC models

Thanks!

Working Paper:

www.ssrn.com/abstract=3622311

Prof. Dr. Dirk Zetsche, LL.M.
ADA Chair in Financial Law (Inclusive Finance)
Head of the Centre for Sustainable Governance & Markets
Faculty of Law, Economics & Finance
University of Luxembourg
Dirk.Zetsche@uni.lu

RUL | RESEARCH UNIT
IN LAW

uni.lu
UNIVERSITÉ DU
LUXEMBOURG

Readings on FinTech

Digital Finance Platforms

www.ssrn.com/abstract=3532975



TechFin / Data-driven Finance

www.ssrn.com/abstract=2959925



Regulatory Sandboxes

www.ssrn.com/abstract=3018534



FT4FI Roadmap

www.ssrn.com/abstract=3245287



Corporate Technologies (AI etc.)

www.ssrn.com/abstract=3392321



Regulating Libra

www.ssrn.com/abstract=3414401



Future of Data-Driven Finance

www.ssrn.com/abstract=3359399



Rise of Tech Risk

www.ssrn.com/abstract=3478640



ICO Gold Rush

www.ssrn.com/abstract=3072298



AI in Finance: Putting Humans

www.ssrn.com/abstract=3531711



Distributed Ledgers / Blockchain

www.ssrn.com/abstract=3018214



eID / KYC Utilities

www.ssrn.com/abstract=3224115

