

MODULE 2 — EU REGULATION: MICA AND FATF STANDARDS

ERCM Jean Monnet Module — Legal Regulation of Crypto-Assets: From Basics to Advanced

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2.1. The Role of MiCAR, Its Main Objectives and Principles for Regulating the Crypto-Asset Market

In February 2017, the European Securities and Markets Authority (ESMA) highlighted, in its report “The Distributed Ledger Technology Applied to Securities Markets,” both the opportunities and the challenges associated with blockchain technologies in the financial securities markets.

In November 2017 and February 2018, ESMA published two statements — on Initial Coin Offerings and a warning on virtual currencies — to alert investors to the high risks associated with these instruments.

In January 2019, as a fully-fledged crypto-asset ecosystem began to take shape, ESMA carried out a comprehensive assessment of the applicability of the EU's existing financial securities rules to this phenomenon, publishing the results in the form of Advice to the EU institutions. The Advice clarified which rules apply to crypto-assets that qualify as financial instruments, and stressed the significant risks arising where crypto-assets fall outside the regulated space.

In order to bring this rapidly developing industry under regulation, on 24 September 2020 the European Commission tabled a legislative proposal for MiCAR (the Markets in Crypto-Assets Regulation) as part of its digital finance package, and on 16 May 2023 the European Union adopted the world's first comprehensive set of rules for crypto-assets in the form of Regulation (EU) 2023/1114 on Markets in Crypto-Assets, known as “MiCAR.”

Regulation (EU) 2023/1114 on Markets in Crypto-Assets (“MiCAR”) establishes uniform EU market rules for crypto-assets. Its provisions apply to crypto-assets that are not currently covered by existing financial services legislation. The key requirements for issuers of and traders in crypto-assets (including asset-referenced tokens and e-money tokens) concern transparency, disclosure, authorization, and transaction oversight.

The new legislative framework is intended to support market integrity and financial stability by regulating public offers of crypto-assets and ensuring that consumers are better informed of the associated risks. The European Union's adoption of the Markets in Crypto-Assets Regulation (MiCA) has been described as a defining moment for the crypto-asset industry. MiCA provides a comprehensive framework for regulating crypto-assets and related service providers across the EU.

ESMA played a significant part in the development of MiCAR — it is an independent EU agency that works to enhance investor protection and promote stable financial markets. Its key functions include:

- Developing technical standards for the regulation of EU financial markets.
- Promoting consistent supervisory and enforcement practices across securities markets.

- Assessing risks to investors, markets, and financial stability.
- Supervising credit rating agencies and trade repositories.
- Coordinating EU-wide supervision of financial market infrastructure.

The objectives of MiCAR are to:

- support innovation and competition in the crypto-asset sector;
- protect holders of crypto-assets;
- address the risks that widespread use of crypto-assets could pose to financial stability and monetary policy.

The core principles underpinning MiCAR's policy are:

- ensuring transparency and stability across the industry;
- establishing an integrated market while fostering a fair and competitive environment;
- protecting consumers and investors;
- establishing a unified approach to digital assets;
- harmonizing European standards for the issuance and circulation of different types of virtual assets;
- protecting the rights of consumers and investors.

2.2. The Concept of Crypto-Assets and Their Categorization

MiCAR defines a crypto-asset as a digital representation of value or of a right that is able to be transferred and stored electronically using distributed ledger technology or similar technology.

Types:

1. The general category of crypto-assets, characterized by a digital representation of value, the ability to be transferred and stored electronically, and the use of distributed ledger technology or similar technology;
2. Utility tokens — crypto-assets intended to provide access solely to a good or service supplied by their issuer;
3. E-money tokens (EMTs) — crypto-assets that purport to maintain a stable value by referencing the value of one official currency;
4. Asset-referenced tokens (ARTs) — crypto-assets that are not EMTs and purport to maintain a stable value by referencing another value or right, or a combination thereof, including one or more official currencies.

MiCAR does not apply to crypto-assets that qualify as financial instruments, deposits, funds, or securitization positions; non-fungible tokens; intra-group services using virtual assets; or crypto-assets issued by central banks or public authorities.

MiCAR imposes stricter requirements on asset-referenced tokens and e-money tokens because of their potential for widespread use as a means of exchange: this could create risks to “the smooth operation of payment systems, monetary policy transmission, or monetary sovereignty,” and therefore requires specific measures to address those risks. For instance, unlike issuers of other tokens, issuers of asset-referenced tokens and e-money tokens must obtain authorization from the competent authority before commencing their activity, with even stricter requirements for tokens designated as “significant.”

Requirements are stricter still for asset-referenced tokens and e-money tokens once they qualify as “significant” — that is, when they meet certain criteria such as “a large customer base, a high market capitalization, or a large number of transactions,” indicating that they are, or are likely to be, used by a large number of people.

2.3. Requirements for Market Participants (Issuers of Crypto-Assets and Crypto-Asset Service Providers (CASPs))

MiCAR applies to natural or legal persons who:

- issue crypto-assets (issuers);
- offer crypto-assets to the public (offerors);
- provide one or more of the following services on a professional basis: custody and administration of crypto-assets on behalf of third parties; operation of a trading platform for crypto-assets; exchange of crypto-assets for funds; exchange of crypto-assets for other crypto-assets; execution of orders for crypto-assets on behalf of third parties; placing of crypto-assets; transfer services for crypto-assets on behalf of third parties; reception and transmission of orders for crypto-assets on behalf of third parties; providing advice on crypto-assets; providing portfolio management on crypto-assets.

Issuers of any tokens must:

be a legal entity;

draw up a crypto-asset white paper in respect of the crypto-assets (a crypto-asset white paper is a detailed document on the issuer, the crypto-asset, its qualitative and quantitative characteristics, a list and description of the rights and obligations attached to the crypto-asset, the risks of the crypto-asset, and so on);

notify the competent authority of the crypto-asset white paper;

publish the crypto-asset white paper accordingly;

comply with requirements on fair disclosure of information about the token, maintain security protocols, bear liability, and so on;

obtain authorization to carry on the activity, completing the authorization process established for the relevant type of issuer.

Depending on the type of token issued, the Regulation also sets out separate requirements on internal organization, the ongoing availability of a certain amount of funds (own funds), and so on.

MiCAR also regulates crypto-asset service providers (CASPs) — those who provide crypto-asset services to clients on a professional basis. The crypto-asset services are listed in Article 3 and include operating a trading platform, custody of crypto-assets on behalf of clients, advice on crypto-assets, and so on.

Requirements for service providers. To provide crypto-asset services, providers must:

- hold authorization from the competent authority of the Member State in which they are established;
- have a registered office in an EU Member State;
- have at least one director resident in the EU.

Obligations of crypto-asset service providers:

- act honestly, fairly, and professionally in the best interests of their clients, and be transparent: provide clients with complete and fair information about their activities and the associated risks, maintain a clear pricing and fees policy, establish complaint-handling procedures, and prevent and manage conflicts of interest.
- meet minimum capital requirements, which vary depending on the specific service provided;
- put in place arrangements and procedures to safeguard clients' ownership rights over the crypto-assets they hold.

Finally, MiCAR also prohibits market manipulation — any activity aimed at artificially influencing the price of crypto-assets. Such conduct may include:

- engaging in transactions or placing orders that give false or misleading signals as to the market, or that fix the price at an artificial level.
- disseminating false or misleading information;
- securing a dominant position over the supply of or demand for a crypto-asset, resulting in the fixing of the price of the crypto-asset or creating unfair trading conditions.