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Markets in Crypto Assets Regulation (MiCAR)

ABC Research Position Paper

The **Austrian Blockchain Center (ABC)** is an interdisciplinary research institute focused on Blockchain and related technologies based in Vienna. Its mission is to be the one-stop-shop Austrian research center for *Blockchain* and related technologies to be applied inter alia in industrial applications, financial services, energy, logistics and government and administrative applications. The COMET centre ABC - Austrian Blockchain Center is funded within the framework of COMET - Competence Centers for Excellent Technologies by BMK, BMDW and the provinces of Vienna, Lower Austria and Vorarlberg. The COMET programme is run by FFG.

The ABC conducts research projects in cooperation with scientific partners, company partners and associated partners (e.g. public institutions). In 2020, ABC started a research project focused on legal aspects of ***Digital Assets based on DLT***¹ in cooperation with the **Vienna University of Economics and Business (WU)** and experts from **leading Austrian law firms**² in the area of digital assets and capital markets.

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I. Preliminary note

The **Austrian Blockchain Center** and the partners of the ***Digital Assets research project*** appreciate the proposed Regulation on Markets in Crypto Assets (MiCAR) as a promising opportunity to promote the use of DLT and strengthen the European Single Market. The draft comprises:

- Minimum disclosure requirements for issuers of all kinds of crypto-assets not yet regulated (Title II)
- Special requirements for the issue of 'stablecoins' (Titles III, IV)
- Requirements for crypto-asset service providers (CASP) (Title V)
- A harmonized framework to ensure consumer and investor protection as well as market integrity, in particular rules on market abuse (Title VI)
- The competence of supervisory authorities (Title VII)

Overall, we see the proposed regulation as a comprehensive and well-drafted approach to promote the use of the DLT, reduce legal uncertainty associated with crypto-assets and ensure consumer protection and financial stability. We believe, however, that the European legislator should put particular **emphasis on a clear and balanced approach** and aim to **prevent disproportionate regulation** that could constitute an obstacle to innovation and is not necessary for the protection of consumers, investors or financial stability. The European legislator may for this purpose want to consider some of the following aspects.

Executive Overview – Position on MiCAR			
Scope of application	Decentralized Finance	'Stablecoins'	Legal concepts and selected provisions
<ul style="list-style-type: none"> scope of application should be balanced to prevent overregulation 	<ul style="list-style-type: none"> create a reliable legal framework for services related to DeFI assets 	<ul style="list-style-type: none"> clearer distinction from financial instruments (MiFID II) necessary 	<ul style="list-style-type: none"> preserve proven regulatory concepts; avoid unnecessary divergences
<ul style="list-style-type: none"> 'catch-all-approach' requires further exceptions (e.g. for NFTs, utility tokens without investment purpose) 	<ul style="list-style-type: none"> clarification to which extent DeFI assets are covered by MiCAR and in which ways service providers (e.g. trading platforms) may provide services related to such assets 	<ul style="list-style-type: none"> Re-evaluation of significance thresholds 	<ul style="list-style-type: none"> provide further guidance on CA-qualification for notification procedure
<ul style="list-style-type: none"> clarification of the scope is necessary, e.g. distinction from regulated assets such as financial instruments 		<ul style="list-style-type: none"> prevention of circumvention practices 	<ul style="list-style-type: none"> removal of the instant-settlement requirement

II. Scope of application

The scope of application is not entirely clear and may be too wide in some cases. This could impede further innovations and may be in conflict with the principle of technology neutrality.

a. General clause definition ('catch-all approach') and exceptions

The definition of 'crypto-assets' laid down in Art 3 (1) (2) adopts a wide '**catch-all approach**'. In principle, we understand and acknowledge the benefits of the approach. A wide scope of application can reduce market fragmentation. It also ensures that market participants can make use of the passporting regime to provide their services across the European Market without national barriers. However, a "catch-all approach" entails the **risk of overregulation** and may provide an obstacle for future innovations that automatically fall within the scope, but are not addressed adequately by the regime. If the approach is maintained, at a minimum particularly **well-drafted exceptions are needed**. To allow for a timely regulatory response to new innovations unintentionally falling within the scope of MiCAR, the Commission could be empowered to specify certain (temporary) exceptions where the application of (certain provisions of) MiCAR is disproportionate.

Furthermore, **technology-neutrality** is a central principle to the regulation of the EU market. As a general principle, we believe that MiCAR should only regulate **assets that are also regulated in the "analog world"** in order to maintain a level playing field.

b. Utility tokens

Title II of the proposed regulation refers to all '*crypto-assets, other than asset-referenced tokens or e-money tokens*'. It therefore covers a wide range of tokens including utility tokens that do not have any investment purposes, even if they are not admitted to trading on a trading platform (e.g. tokenized tickets for cultural events; tokenized vouchers for DLT or electronic services such as digital file storage or streaming services). We perceive no reason to regulate the offer to the public of such utility tokens. Furthermore, issuance and trading of comparable assets not issued using the DLT (e.g. electronic vouchers) is not regulated. We therefore suggest **exempting utility tokens without any investment purpose**, at least if they are not admitted to

trading on a trading platform. We also suggest a careful re-evaluation, if and to which extent the admission to trading of such assets should be regulated.

Regarding **utility tokens with investment purpose**¹, there are different views of the NCAs of the member states if they constitute financial instruments. We thus recommend a **clarification** that utility tokens that do not comprise any entitlement to the future payment of money (legal tender) or monetary surrogates (e.g. payment tokens) are not financial instruments pursuant to MiFID II², but are solely regulated under the MiCAR regime.

c. 'Non-fungible tokens' (NFTs)

Since the commission draft of MiCAR has been published, '*non-fungible tokens*' have become more important. The potential use cases go far beyond digital art and may comprise copyright enforcement, real estate as well as digital and tangible collectibles. Due to their non-fungible nature, we believe that deviations from the regulatory approach of MiCAR are necessary. The commission draft regulation, however, only exempts NFTs from provisions of Title II.³ In light of the nascent stage and huge potential of NFTs, we suggest excluding them entirely from the scope of application. This restriction could be achieved, for example, by **adapting the current definition of 'crypto-assets'**. Nevertheless, the application of the MiCAR regime on fungible **NFT-fractions** with values exceeding certain thresholds may be adequate.

d. 'Hybrid tokens', 'stablecoins' and financial instruments

Another aspect of concern is the unclear distinction between **financial instruments** (as defined in MiFID II) and some crypto-assets.

Although there is a general exception of financial instruments in Art 2 (2) MiCAR, further clarification of the classification of **hybrid tokens** is necessary. Such tokens may have components of both, utility tokens as well as a security tokens. For example, a token may entitle the token-holder to repayment of the principal amount of EUR 1 + 20% interest after five years or alternatively allows to use the issuers DLT file storage for one month. In our view, if such tokens share key characteristics of financial instruments (e.g. payment of dividends or interest), they should only fall within the scope of MiFID II and not MiCAR.

Furthermore, certain '*stablecoins*' in the form of asset-referenced-tokens may be considered financial instruments at least in some member states. The **classification of ART** should be clarified to avoid potential overlaps.

III. Decentralized Finance

Decentralized finance (**DeFi**) has been a key driver for the DLT. In particular, assets based on decentralized systems that do not have a single identifiable issuer, such as Bitcoin and Ether, have been the success factor for crypto-assets in the past. In our opinion, a **reliable legal**

¹ See Art 4(3) MiCAR: '[...] *utility tokens for a service that is not yet in operation* [...]'.

² Directive 2014/65/EU on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

³ Art 4 (2) (c) MiCAR.

framework for services related to DeFi assets (and DeFi services) is essential for the DLT market. Services relating to DeFi assets should, of course, remain regulated under Title V of the proposal. However, Title II and Art 68 (1) are missing a central connecting factor, as there is no legal entity that issues and admits to trading such assets. The grandfathering clause provided in Art 123 (1)⁴, on the other hand, would only allow for the provision of services related to already established assets⁵, while at the same time barring comparable innovative concepts. In this respect, we would encourage **clarification** to which extent DeFi assets are covered by MiCAR and in which ways service providers (e.g. trading platforms) may provide services related to such assets. Considering the importance of DeFi assets for the development in the past, we believe that an outright ban of (services related to) such assets is not in the interest of the European Union.

IV. Stablecoins

MiCAR puts a main focus on the regulation of ‘*stablecoins*’. Besides the unclear distinction from financial instruments mentioned above, it is unclear if the **significance thresholds** are adequate. While the commission states that stablecoins currently do not pose a threat to financial stability,⁶ various stablecoins already on the market may be considered significant. Before the final draft, the European Legislator should thoroughly evaluate the thresholds or make them more flexible in order not to establish unnecessary barriers adversely affecting the market.

Another potential issue is the **delineation of ARTs and EMTs**. In light of MiCAR's different levels of regulatory requirements for ARTs and EMTs, circumvention practices (e.g. ARTs with disproportionately high weight on a single fiat currency i.e. an ART refers to the value of EUR [99%] and Ether [1%]) may pose a potential threat. Therefore, we would mandate a **clearer distinction** between the individual ‘*stablecoins*’.

V. Consistency with financial markets regulations

MiCAR contains many legal concepts already known from financial markets regulations such as MiFID II, MAR⁷ and the PR⁸. We acknowledge that, for various reasons, crypto-assets may intentionally be regulated differently compared to financial instruments. However, the proposed regulation differs from proven legal concepts in many provisions for no apparent reason. Incautious deviations from proven concepts, however, may cause unintended side effects. For example, the definition of ‘issuer of crypto-assets’ in Art 3 (1) (6) is not consistent with the notions of ‘offeror’, ‘issuer’ and persons seeking admission to trading in the PR. Furthermore, the deviation of Art 14 MiCAR from Art 11 PR, indicating a mandatory direct

⁴ Art 123(1): “Articles 4 to 14 shall not apply to crypto-assets other than asset-referenced tokens and e-money tokens, which were offered to the public in the Union or admitted to trading on a trading platform for crypto-assets before [date of entry into application].”

⁵ It is unclear, however, if this exemption also applies to crypto-assets that are already admitted on trading venues if they shall be admitted to trading on an additional trading venue.

⁶ Recital 4 MiCAR.

⁷ Regulation 2014/596/EU (Market Abuse Regulation).

⁸ Regulation 2017/1129/EU (Prospectus Regulation).

liability of the issuer's management body towards the holders of the crypto-assets, is not in line with the implementation of the PR in some member states and may constitute a significant impediment. We thus strongly support a full alignment with proven concepts and recommend **departing from existing regulatory concepts only in cases where a different approach is intended and necessary**.

VI. Notification

According to Art 7 (1) MiCAR, the draft stipulates a **notification** of the crypto-asset white paper prior to its publication. No stricter form - such as the approval of the supervisory authority - is required. According to Art 7 (3), the notification of the whitepaper shall also explain why the crypto-asset described therein is not to be considered a regulated asset under other regulations.⁹ We generally support this approach and believe that this is a well-balanced solution for non-financial assets. However, this explanation could still pose a challenge to the issuer considering the difficult qualification of crypto-assets in some cases (see the remarks on 'hybrid tokens' and 'stablecoins' above). We would thus encourage the publication of further guidance (e.g. **guidelines and Q&As**) in order to support issuers and NCAs.

VII. Instant on-chain settlement

Art 68 (8) requires crypto-asset services providers operating a trading platform to complete the final settlement of a crypto-asset transaction on the DLT on the same date the transaction has been executed on the trading platform. While instant-settlement may have advantages and may be desirable sometime in the future,¹⁰ the **requirement of instant-settlement is not in line with the current state of the art and the current market practice**. The majority of CASPs, including the industry's largest players, are organized as centralized trading platforms offering several services, including trading platform services, purchase and sale and/or custody in relation to crypto-assets. In particular, this means that clients' assets are generally stored via wallets of the CASP (omnibus account) and trades are recorded on internal databases only. On-chain settlement only takes place if the client decides to withdraw the corresponding amount of crypto-assets and transfer the assets to an external wallet.

Instant on-chain settlement is, at the current state of art, neither technically feasible, nor is it in the interest of clients and CASPs. In particular, a corresponding requirement could inhibit small transactions due to the **transaction fees and technical restrictions of many current DLT systems**. We therefore suggest **abandoning the requirement for instant on-chain settlement** and, instead, require the CASP to settle the transactions on-chain only upon withdrawal within a reasonable amount of time.

⁹ E.g. lit a) as a financial instrument or lit b) as electronic money.

¹⁰ Note that this is discussed for **transferable securities** where the current legal requirement for the **settlement date is T+2** according to Art 5 (2) CSDR.