

P.R.I.M.E. Finance

Panel of Recognized International Market Experts in Finance

Regulation of Crypto-Assets in the European Union and in France



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Hubert de Vauplane

Partner, Kramer Levin Naftalis & Frankel LLP (Paris)

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ESMA and EBA reports (legal qualification)

January 9, 2019: ESMA and EBA publish reports on crypto-assets

- Clarification of the application of existing EU rules to crypto-assets
- Advice to the European Commission on the regulatory issues raised by crypto-assets

Main findings regarding the legal qualification of crypto-assets:

- 1. EBA:** only the qualification of electronic money (EMD 2) may apply to redeemable fiat-backed stablecoins
- 2. ESMA:** certain kind of crypto-assets may qualify as financial instruments (MiFID II) and/or transferable securities (subcategory of financial instrument)
 - **Condition:** existence of profit rights attached to the token, even though ownership or governance rights may not necessarily exist
 - Pure utility tokens may fall outside of the existing financial regulation
 - Payment/exchange tokens (*i.e.* Bitcoin, Litecoin, Ether, etc.) would be unlikely to qualify as financial instruments

If crypto-assets qualify as financial instruments, numerous EU rules would apply

- Prospectus Directive, Transparency Directive, MiFID II and MiFIR, Market Abuse Regulation, etc.



ESMA and EBA reports (advices)

Advices to the European Commission:

- AML/CFT: extend (again) the scope of the 5th Anti-Money Laundering Directive to crypto-to-crypto exchanges and providers of financial services for ICOs (in accordance with the recommendations of the FATF in October 2018)
- When crypto-assets qualify as financial instruments: need to amend the EU legislation to clarify how it applies to this new asset class
- EBA will monitor the use of crypto-assets by regulated financial institutions and is working with the Basel Committee on Banking Supervision to clarify the prudential treatment of banks exposed to crypto-assets
 - Accounting rules related to crypto-assets will need to be clarified and standardised

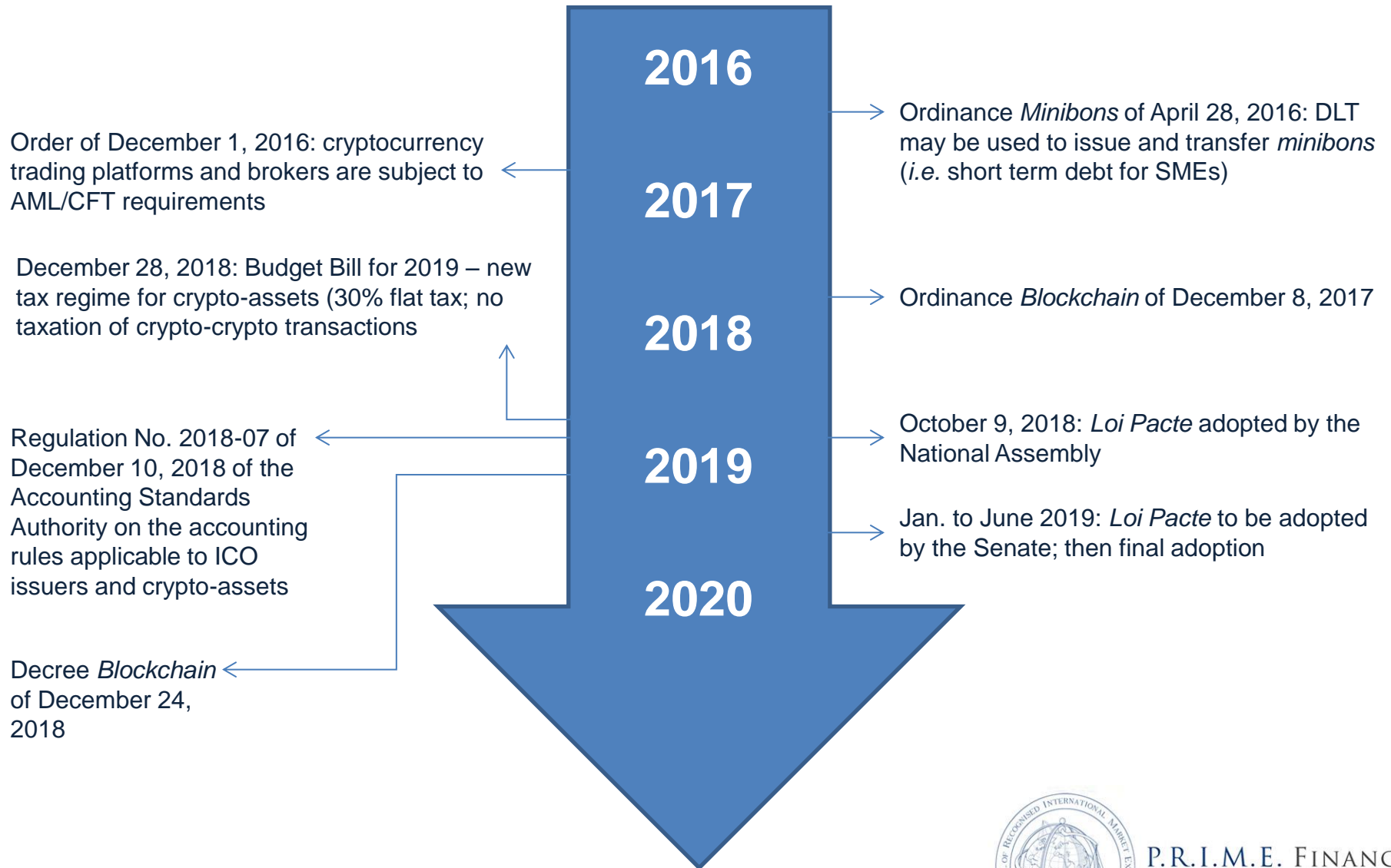
Ongoing creation of bespoke regulatory regime in EU countries (France, Malta):

- ESMA considers that an EU-wide approach is the most appropriate response
- Risks of uneven playing field and regulatory arbitrage
- Still, ESMA does not support the elaboration of an EU bespoke regime for crypto-assets which do not qualify as crypto-assets => risks of “legitimizing” crypto-assets and encouraging wider adoption

EU countries will probably keep developing national regimes because there is a need for (i) consumer protection and (ii) clear rules encouraging the development of a sound crypto-industry



Regulation of crypto-assets in France: a chronology



The Loi Pacte: an overview

Outspoken goal of the French government: become a hub for ICOs and a world leader in the regulation of crypto-assets

Calendar:

- October 2018: Loi Pacte voted by the National Assembly
- January/February 2019: Loi Pacte discussed by the Senate
- ~May/June 2019: final version of the bill adopted
- Summer 2019: update of the General Regulation of the AMF

Overview:

- Optional visa of the AMF for compliant ICOs
- Regulatory framework for crypto-intermediaries (e.g. exchanges, custodians, ICO investment advisors)
- Right to open a bank account for approved ICOs and authorized crypto-intermediaries
- Certain regulated investment funds will be able to invest in crypto-assets



Optional visa for compliant ICOs (1)

France has not been a major hub for ICOs: only €89m raised as of November 2018

Scope of the new regime: will not apply to tokens which share the same characteristics as financial instruments => offerings of “security tokens” would have to comply with existing regulations

Optional visa of the AMF: token issuers will be free to apply for the visa or proceed without it

AMF's rationale:

- Token issuers will be able to market more easily their ICOs in France
- The global reputation of the AMF will help token issuers to market their ICOs in foreign jurisdictions
- The AMF's visa will mean that the project is promising and the team is trustworthy



Optional visa for compliant ICOs (2)

Conditions to obtain the AMF's visa:

- The issuer is a legal entity incorporated in France (or registered in France through a branch)
- The disclosure document (*i.e.* the white paper) and the marketing materials are accurate, written in plain language, and non-misleading; they describe the risks associated with the offer
- The issuer plans to implement adequate procedures to track and safeguard the funds raised in the ICO

The General Regulation of the AMF will detail the approval procedure and the required supporting documents, as well as the expected content of the white paper.

- The AMF has already started drafting these provisions => the goal is to be able to start processing ICO projects shortly after the Loi Pacte passes into law



Bespoke regime for crypto-intermediaries (1)

Creation of a new category of regulated service providers: **digital assets services providers**

Wide definition of digital assets: all crypto-assets would qualify as digital assets (including ICO tokens, except those which qualify as financial instruments)

Services related to digital assets would include various kinds of traditional investment services, as soon as they are performed in relation with digital assets:

- Custody of digital assets or cryptographic private keys for third parties
 - **NB:** ongoing debate among stakeholders regarding the concept of custody with respect to crypto-assets => what is actually kept by the custodian?
- Purchase or sale of digital assets against fiat currency
- Purchase or sale of digital assets against other digital assets
- Operation of a digital assets trading platform
- Various other services (when related to digital assets): receipt and transmission of orders on behalf of third parties, asset management, investment advices, underwriting, placing with or without a firm commitment



Bespoke regime for crypto-intermediaries (2)

As for the AMF's visa, the idea is to make the license **optional**. More specifically:

- **Mandatory registration** for custodians and fiat-crypto exchanges
- **Optional license** for all other activities defined as digital assets services

Conditions for the optional license:

- Subscription to a professional liability insurance (or comply with capital requirements)
- Resilient IT systems
- Set out (i) adequate security procedures, (ii) internal audits, (iii) policies to manage conflicts of interests
- Other requirements depending on the service provided, e.g. custody policy and implementation of segregated accounts for custodians

AML/CFT requirements will apply to (i) registered digital assets custodians and fiat-crypto exchanges and (ii) other digital assets service providers which obtained the optional license.



Right to open a bank account

Very common issue for ICO issuers/crypto-intermediaries: **very difficult to open a bank account in France and access basic banking services**

- Need to solve that issue to become a crypto hub

Description of the right to a bank account in Loi Pacte: banks will have to set up objective, non-discriminatory and proportionate rules when deciding to open a bank account for the following actors:

- Token issuers which have been granted an optional approval by the AMF
 - Registered digital assets custodians and fiat-crypto exchanges
 - Other digital assets service providers which obtained the optional license
- **Strong incentive** to apply for an optional AMF's visa or license
 - Same categories as those subject to AML/CFT requirements

Further provisions:

- Once the account is open, access to basic banking services shall not be limited
- If a bank denies an entity mentioned above the right to open an account, it shall communicate the reason of such refusal to the AMF or the ACPR. Entities denied a bank account may also appeal against the bank's decision
- Last resort if obstruction from banks: entities may open a bank account in the books of the Caisse des dépôts et consignations
 - This provision will likely be removed by the Senate



Beyond crypto-assets: tokenized securities

Since December 2018, the use of a distributed ledger (formally denominated “shared electronic recording system” or DEEP in French) for the issuance, registration and transfer of unlisted securities is now allowed under French law.

The distributed ledger must comply with **four technical conditions**:

- The DL must be “conceived and implemented” in a manner which preserves the integrity of the information recorded
- The DL must allow “directly or indirectly” the identification of the owners of the securities
- A business continuity plan, which includes an external data recording system, must be set out
- Owners of the securities registered on the DL must be able to access their statements of transactions.

Fundamental questions raised by this new regime:

- Are securities registered on a distributed ledger **tokenized securities** or **security tokens**?
- Can both **private and public blockchains** be used to issue and register securities?
- If a public blockchain is issued, **who is responsible** for the compliance with the requirements?

