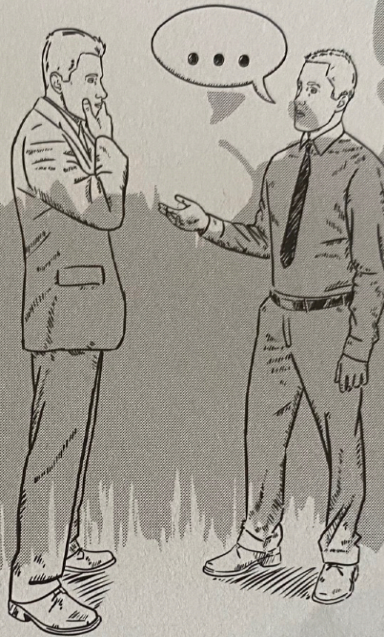


Managing Risks Emanating from Privat-sector Crypto Assets

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AT A PARTY



Two businessmen meet at a party and discuss their businesses.
“There are many ways to make money,” one says, “but there’s only one honest way.”
“Really?” says the other one. “What’s that?”
“Interesting that you don’t know it!” the first man replies.

Monday

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Types of Risks Emanating from Private-sector Crypto Assets

- **Regulatory and supervisory gaps:**
 - Threats to global financial stability;
 - Gaps re. protection of investors.
- **Private law aspects:**
 - Certainty and enforceability of individual investors' legal position;
 - Applicable insolvency law;
 - Large-scale failures threat to global financial stability.

Regulatory and Supervisory Enhancement

View of Global Standard Setters

- **Global market share:** Private sector Crypto Asset volumes are still relatively small compared to the global financial system
 - Total market capitalisation around US\$ 2.5tn compared with US\$ 22 tn for the S&P500 ;
 - Daily trading volumes up to US\$ 175bn.
- **Joint opinion so far: Currently no threat to global financial stability.**
- **FSB warning** (February 2022 report):“Crypto Assets are fast evolving and could reach a point where they represent a threat to global financial stability.”

EU/EEA Regulatory System: Product – Related Application

Financial
instruments

Electronic
money

None of the
foregoing

Current EU/EEA Regulation of Crypto-Assets

EU/EEA regulatory baseline: substance over form

- Crypto-assets classified as Financial Instruments under MiFID II Directive (2014/65/EU): set of related regulatory frameworks applied;
- Crypto-assets classified as e-money: related regulatory framework applied;
- Crypto-assets not classified as Financial Instruments or e-money: certain national regulations by Member States may apply.

National Regulation of Crypto-Assets

EAA: Liechtenstein - Comprehensive legal framework in force

- Token and TT Service Provider Act (TVTG, 3rd Oct. 2019);
- Regulation on Token and TT Service Providers (TVTV, 16th Dec 2019).

Switzerland: Comprehensive legal framework in force

- Blanket framework, based on specific amendments to several federal acts.

EU Regulatory System:

Crypto Assets in Portfolios of Regulated Institutions

- Current EU law does not prohibit financial institutions, including credit institutions, investment firms, payment institutions and electronic money institutions, from holding or gaining exposure to Crypto Assets or from offering services relating to Crypto Assets.



Crypto Assets in portfolios of regulated institutions: general supervisory risk assessment and internal risk processes applied.

- **BCBS** is quantifying the materiality of banks' direct and indirect exposures to Crypto Assets, clarifying the prudential treatment of such exposures.

EU Regulatory System: AML and Combat of Terrorism Financing

Permanent Adaptation to FATFA Recommendations

E U AML Directive now includes as „obliged entities“:

- **Providers engaged in exchange services between virtual currencies and fiat currencies;**
- **Custodian wallet providers**

EU/EEA Future Regulation of Crypto-Assets

Regulatory package

- Addendum to MiFID II Directive: clarification that existing definition of „financial instruments“ includes „instruments issued by means of DLT“ (to be transformed into national law);
- Regulation on Markets in Crypto-Assets („MiCA“) to cover crypto-assets falling outside existing EU financial services regulation, including „stablecoins“ and e-money tokens (direct force of law in Member States) - publication in EUOJ early 2023, applicable 12/18 months thereafter (2024);
- Security Tokens representing traditional financial instruments: application of MiFID;
- Regulation on a Pilot Regime for Market Infrastructures based on DLT (direct force of law in Member States) – Regulation (EU) 2022/858, applicable from 23rd March 2023;
- „EU Passport“ for crypto-assets.

EU Regulatory Package: MiCA

MiFID-type regulation

- Regulated asset categories: asset-referenced tokens („stablecoins“), electronic money tokens, utility tokens);
- Regulated activities: issuers of regulated asset categories and crypto-asset service providers;
- Specific regulations:
 - Crypto Assets other than asset-referenced tokens or e-money: offers to the public/admission to trade on a trading platform restricted to legal entities; compliance obligations and liabilities of issuers.
 - „stablecoins“: issuers restricted to EU residence; licence and minimum own funds; regulations on reserve assets backing tokens; additional requirements for issuers classified as „significant“.
 - Electronic money tokens: subject to enhanced requirements (e.g. licence as credit or electronic money institution).
 - Crypto Asset Service Providers: restricted to legal persons with EU residence; licence + minimum own funds; comprehensive compliance requirements.
 - General provisions re. prevention of market abuse; administrative sanctions.

EU Regulatory Package: Pilot Regime

Operating conditions for DLT market infrastructures, „sandbox approach“

- Application:
 - Crypto Assets qualifying as financial instruments /transferable securities under MiFID II;
 - Market infrastructure participants (investment firms, market operators, central securities depositories).
- Restricted to multilateral trading facilities (MTFs) and Securities Settlement Services.

Private Law Aspects

Certainty and enforceability of individual investors' legal position

- Private law not covered by international or EU/EEA harmonisation
 - Subject to national law and application by national courts.
- Consequences of classifying Crypto Assets as property:
 - Eligibility for creation of security interest, lien or usufruct;
 - Eligibility to be held in trust;
 - Segregation in the bankruptcy estate of a wallet or custody services provider;
 - Segregation in a heritage estate.
- Legal status of DLT/Blockchain technology recognised as documentary evidence?
- Legal formalities applied to transfer of Crypto Assets backed by legal recognition?

Common Law Jurisdictions

Principles-based concept of property allows for flexibility to include Crypto Assets

- Groundbreaking: UK Jurisdiction Taskforce study „Legal Statement on Cryptoassets and Smart Contracts“ (2019)
 - Not legally binding, but theoretical basis for the concept of property re. Crypto Assets in the Common Law community;
 - Principles adopted by several high court judgements.
- Basis: criteria as defined by Lord Wilberforce (National Prime Bank vs. Ainsworth (1965) AC 1175, at 1247-1248).

Civil Law Jurisdictions

Absolute rights that can be asserted against anyone normally restricted to an exhaustive number of separate property rights („numerus clausus“) – conclusion not uniform, depending on individual legal systems

- Comprehensive legislation defining property rights, legal status of DLT/Blockchain technology and legal formalities applied to transfer of Crypto Assets : Liechtenstein and Switzerland;
- Heading towards specific legislation: e.g. Germany - Law on e-securities (eWpG) covering crypto assets, but restricted to bearer bonds + units in common funds (KryptoFAV). Crypto Assets classified as moveables (chattel).
- Court cases affirming property rights re. Crypto Assets: Italy, Netherlands, Russia.
- Court cases rejecting property rights re. Crypto Assets: Japan, Spain.

Conclusion: Jurisdiction Matters

Clear choice of law and court in private-sector Crypto Asset frameworks essential.

Note: Applicable insolvency law not subject to agreement by the parties involved.

Many thanks for your attention

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