



MiCA explained: the EU crypto-asset law

The proposed Markets in Crypto-assets Regulation

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Abbreviations

AML	Anti-money laundering
CASP	Crypto-asset Service Provider
CFT	Countering the financing of terrorism
DeFi	Decentralised Finance
DLT	Distributed Ledger Technology
E-money	Electronic money
EBA	European Banking Authority
EEA	European Economic Area (comprising the EU countries and also Iceland, Liechtenstein and Norway)
ESMA	European Securities and Markets Authority
EU	European Union (comprising Austria, Belgium, Bulgaria, Croatia, Republic of Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain and Sweden)
MiCA	Markets in Crypto-assets Regulation

Executive Summary

The European Commission's Digital Finance Package was adopted on 24 September 2020 and includes, among several significant new strategies and proposals, a proposed Regulation on crypto-assets, the **Markets in Crypto-assets Regulation**. MiCA will be **directly applicable throughout the EEA, superseding any national regimes** relating to crypto-assets. AML/CFT legislation is unaffected.

This comprehensive and stringent framework introduces **significant regulatory control** and oversight of **previously unregulated** areas of a crypto-asset industry that has, at times, seen both fraud and market abuse. Complying with MiCA, however, **may present significant challenges**, especially for those involved with **DeFi** projects.

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

MiCA primarily focuses on the **issuance** of crypto-assets and the provision of **crypto-asset services**. MiCA defines a crypto-asset as *a digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology*. Certain provisions apply to **all crypto-assets** including, notably, **utility tokens**. More stringent requirements, however, apply to **stablecoins** which are categorised as either **asset-referenced tokens** or **e-money tokens**. The most stringent requirements are reserved for stablecoins that are designated by the European Banking Authority as **significant**.

Issuers of crypto-assets will, among other obligations, be required to be **incorporated as a legal entity**, to produce and publish a **whitepaper** ahead of any issuance, and to adopt **standards on marketing**. Whitepapers must contain **prescribed minimum information** but do not need to be approved in advance unless they relate to asset-referenced tokens or e-money tokens. Issuers of asset-referenced tokens and e-money tokens will **need to be authorised** by a regulator.

MiCA introduces a broadly defined set of activities for which **crypto-asset service providers** must be authorised. CASPs will need to comply with regulatory provisions **similar to traditional financial services** firms such as conduct, customer asset safeguarding, market abuse and prudential requirements. Like issuers, CASPs must be established as legal entities.

The European Commission's proposed Regulation will now go through legislative deliberations that, typically, take between one and three years to complete.

Although MiCA will not apply immediately, crypto-asset issuers and service providers should start becoming familiar with its **requirements** and to consider the potential **implications** of this comprehensive regime so as to **plan for the future**.

MiCA will have a profound impact on crypto-assets, both in the EU and across the world.

Introduction

On 24 September 2020, the European Commission published a proposed regulation on **Markets in Crypto-assets**, a momentous legislative framework to regulate, for the first time in the EU, all forms of crypto-assets as well as a wide range of crypto-asset services. While crypto-assets that fall in scope of other EU legislation (e.g., the Markets in Financial Instruments Directive) will continue to be regulated under those frameworks, MiCA covers all other **crypto-assets and related activities that are currently unregulated**. No stone has been left unturned. Notably, MiCA introduces requirements relating to the **issuance, offering and marketing** of crypto-assets, the **authorisation and operation** of crypto-asset service providers, and the **prevention of market abuse**.

MiCA forms part of a broad new **Digital Finance Package**, adopted by the European Commission at the same time, that aims to promote **innovation and competition** in the EU financial sector, for the benefit of citizens and businesses alike, while **protecting consumers and investors**, and ensuring **market integrity and financial stability**. The Commission believes MiCA's regulatory requirements will achieve these objectives and provide much-needed **legal clarity** to the crypto-asset industry.

Additionally, the Commission has sought to **harmonise the EU framework with the Financial Action Task Force's Recommendations** through the alignment of terminology and scope of application, a step it believes is crucially necessary to tackle the risks associated with regulatory arbitrage. As an EU Regulation, MiCA will be **directly applicable across the EEA** without the need for further national legislation, establishing a common framework and avoiding anomalies resulting from different national interpretations.

CASPs (i.e., those who provide crypto-asset services) will be **authorised by national regulators** (referred to as *competent authorities* in MiCA) and will be able to **provide their services throughout the EEA**, a process known as *passporting*.

Consumer and investor protection is the primary focus in MiCA. In particular, requirements aimed at increasing **transparency and regulatory oversight** are intended to **level the playing field** between the traditional and crypto-asset industries, although some provisions may **unintentionally favour market incumbents**. These measures will likely mitigate against **consumer and investor harm** resulting from prevalent **market manipulation and fraud** that has largely gone unchecked due to a **lack of regulation**. The protection of consumers and investors and the introduction of measures to ensure market integrity will help **build trust** in crypto-assets with both consumers and institutions, and may ultimately lead to more widespread use of crypto-assets and distributed ledger and blockchain technologies that underpin many of them.

Requirements in MiCA relating to the **offering and marketing** of crypto-assets particularly seek to address these objectives. However, the obligation that **crypto-asset issuers must be incorporated in the form of a legal entity** could **pose significant challenges for DeFi projects** where issuance is decentralised and there is no identifiable issuer. So, while MiCA may, generally, promote consumer and investor protection, market integrity and financial stability, some innovative areas, such as DeFi, may face significant and **irreconcilable regulatory challenges** and possible existential questions, at least in Europe.

MiCA may also, unintentionally, **stifle innovation and competition** or **drive out of Europe** small new technology firms that do not have the resources to meet MiCA's stringent requirements.

Some **traditional financial services firms** that will not require separate authorisation to provide crypto-asset services under this Regulation, may enjoy **competitive advantage** over CASPs that have to wait to be authorised under MiCA.

One type of crypto-asset singled out for special treatment is **stablecoins** which are categorised as either **asset-referenced tokens** or **e-money tokens**. Each category is subject to its own more stringent set of requirements than apply to other crypto-assets such as utility tokens. The most stringent requirements are reserved for asset-referenced tokens and e-money tokens that are deemed **significant**.

The European Commission's proposed Regulation will now be deliberated on by the European Parliament and the Council of the European Union, and then between the three institutions, a process that can take anything **between one and three years** overall. Once MiCA comes into force, Member States and their regulators will have 18-months in which to operationalise the regime. At the end of the 18-month period, MiCA will apply to issuers and CASPs. However, issuers of e-money tokens and asset-referenced tokens, will not benefit from this 18-month period and will be required to comply immediately MiCA comes into force.

MiCA is, for some, the much-needed **comprehensive legislation** they have long waited for. It will have a **profound impact on crypto-assets and crypto-asset services** not just in Europe but **throughout the world** as nations outside the EEA seek to catchup and, to some extent, **emulate MiCA** in their own jurisdictions.

This report aims to provide a detailed summary of the proposed MiCA. It is not an exhaustive analysis and is, therefore, purely indicative. **This report does not constitute legal advice and should not be relied upon.** It sets out MiCA's most important requirements, providing an overview of each section or Title, as well as some implications for the crypto-asset industry. MiCA will undoubtedly be **subject to amendment** as it progresses through the EU legislative process.

Title I: Subject Matter, Scope and Definitions

Article 1: Subject Matter

Several widely applicable, uniform requirements are established by MiCA to ensure a broad scope of application to the crypto-asset industry. These requirements cover the following subjects outlined under Article 1:

- a) transparency and disclosure;
- b) authorisation and supervision;
- c) operation, organisation and governance;
- d) consumer protection;
- e) prevention of market abuse.

Transparency and disclosure requirements will apply to both the issuance and admission to trading of crypto-assets, which has been largely unregulated across the EU except in certain jurisdictions where regulations are in place for activities such as Initial Coin Offerings (ICOs), or where the crypto-asset meets the definition of a financial instrument, meaning it is already captured under the current EU framework and not in scope of MiCA.

Requirements relating to **authorisation and supervision**, as well as to **operation, organisation and governance**, will apply to a) CASPs; b) issuers of asset-referenced tokens; and c) issuers of electronic money tokens.

Consumer protection requirements will apply to the issuance, trading, exchange, and custody of crypto-assets, thus aiming to secure a safe environment for consumers at each stage of their interactions with crypto-assets.

Further, measures to ensure the **prevention of market abuse** will be introduced by MiCA in order to protect the integrity of crypto-asset markets, including requirements for CASPs to monitor, detect and report market abuse.

Article 2: Scope




MiCA applies to entities which are engaged in the issuance of crypto-assets and the provision of crypto-asset services within the EU, although there are several exemptions to its broad scope of application which are listed below.

However, these exemptions do not necessarily indicate that the relevant activity is unregulated, as most of the exemptions relate to activity which is already regulated under other legislation.

Article 2(2) lists those crypto-assets which fall within the scope of other legislation and are **exempt from MiCA**:

- (a) **financial instruments** (as defined under the Markets in Financial Instruments Directive II¹ (MiFID II) Article 4(1)(15));
- (b) **electronic money** (as defined under the E-Money Directive² Article 2(2)) except if qualified as an electronic money token under MiCA;
- (c) **deposits** (as defined under the Deposit Guarantee Schemes Directive³ Article 2(1)(3));
- (d) **structured deposits** (as defined under MiFID II Article 4(1)(43));
- (e) **securitisation** (as defined under the Securitisation Regulation⁴ Article 2(1)).

Under Article 2(3), **various entities and persons are exempt from MiCA** in some circumstances, including the ECB, insurance undertakings, and liquidators. Further, the authorised firms listed below are exempt from certain MiCA provisions:

 <p>Credit institutions authorised under the Capital Requirements Directive IV⁵ when issuing asset-referenced tokens or providing crypto-asset services</p>	 <p>Investment firms authorised under MiFID II when only providing crypto-asset services equivalent to the investment services and activities for which they are authorised under MiFID II</p>	 <p>Payment institutions authorised under the Payment Services Directive 2⁶ when providing payment services with crypto-assets</p>
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Traditional financial institutions may enjoy a competitive advantage in the wake of MiCA's stringent regulatory requirements, as they may be able to provide crypto-asset services without needing to be authorised under MiCA.

¹ Directive 2014/65/EU.

² Directive 2009/110/EC.

³ Directive 2014/49/EU.

⁴ Regulation (EU) 2017/2402.

⁵ Directive 2013/36/EU.

⁶ Directive (EU) 2015/2366.

Article 3: Definitions

MiCA provides an extensive list of definitions relating to crypto-assets under Article 3(1), including, most notably:

- a) **crypto-asset:** a digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology;
- b) **asset-referenced tokens:** a type of 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;
- c) **electronic money (e-money) token:** a type of 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;
- d) **crypto-asset service provider:** any person whose occupation or business is the provision of one or more crypto-asset services to third parties on a professional basis;
- e) **crypto-asset service:** any of the services and activities listed in paragraph 9 of Article 3(1) relating to any crypto-asset, including custody and exchange services.

While crypto-asset related terminology and definitions have often diverged across the EU, those provided by MiCA support regulatory harmony in the EU crypto-asset industry. For example, the alternative terms to 'crypto-asset' used across the EU in recent years include 'virtual asset', 'virtual currency', 'digital currency', and 'cryptocurrency'. Also, the term 'stablecoin' has frequently been used to refer to assets which constitute an 'asset-referenced token' or an 'e-money token' under MiCA. Further, persons defined in MiCA as a 'crypto-asset service provider' have often been referred to as a 'crypto-asset business' or a 'virtual asset service provider' (VASP).

Under Article 3(2), the European Commission has the power to adopt delegated acts to adjust these definitions in line with developments in markets and technology. This can ensure that **MiCA continues to be broadly and uniformly applicable**, including to new innovations in this sector. For example, the already lengthy list of crypto-asset services may be extended to include new types of services as they emerge.

Crypto-asset services under MiCA Article 3(1)(9)



MiCA's comprehensive list of crypto-asset definitions and services will support the broad and uniform application of MiCA across the EU. Further, the flexibility for amendments to MiCA will be key in maintaining its widespread application in line with future industry developments.

Title II: Offering and Marketing of Crypto-Assets

To offer and market crypto-assets in the EU, issuers must be incorporated as a legal entity and must publish a whitepaper prepared in accordance with Article 5.

An issuer can take advantage of certain **exemptions**, including where:



The requirement for issuers to be incorporated as legal entities could have a significant impact on DeFi projects, which aim to leverage DLT to allow for peer-to-peer finance. Issuers of such tokens are at times unidentifiable, meaning that requiring these projects to establish as legal entities poses existential questions to DeFi.

MiCA sets a number of common requirements across issuers, not only of crypto-assets which are covered by Title II, but also of asset-referenced tokens (Title III) and e-money tokens (Title IV).

For example, under Article 13(1), issuers are required to:

- a) act **honestly, fairly and professionally**;
- b) communicate with the holders of crypto-assets in a **fair, clear and not misleading manner**;
- c) prevent, identify, manage and disclose any **conflicts of interest** that may arise;
- d) maintain all of their **systems and security access protocols** to appropriate Union standards.

Further, there are a number of **consumer protection provisions** under MiCA, such as a requirement for issuers of crypto-assets to act in the **best interests of the holders of crypto-assets**. This requirement further mandates that no purchaser of crypto-assets shall obtain **preferential treatment** as regards one another, unless such preferential treatment is **disclosed in the whitepaper** published by the issuer.

This requirement will ensure that issuers are unable to offer large discounts to early purchasers of tokens without fully disclosing the terms that they were issued under. Many of the early token sales would involve a private sale with a substantial discount to the initial (often institutional) backers of a project.

Issuers that set a **time limit** for their offer to the public are also required to have effective arrangements in place to **monitor and safeguard the funds**, or other crypto-assets, raised during the offer. This means that the funds or other crypto-assets collected during the offer to the public must be **kept in custody** by either:

- a) a credit institution, where the funds raised during the offer to the public take the form of fiat currency;
- b) a crypto-asset service provider authorised for the custody and administration of crypto-assets on behalf of third parties.

This would transform the way in which token sales are undertaken and could be hugely problematic if the funds cannot be held in a smart contract deployed by the issuer.

Where an offering of crypto-assets is **cancelled** for any reason, the issuer needs to ensure that any funds collected from the purchasers are **returned to them** as soon as possible.

The whitepaper

A whitepaper needs to include the following information outlined under Article 5(1):

Fair, Clear, Not misleading

- (a) a detailed description of the issuer and a presentation of the main participants involved in the project's design and development;
- (b) a detailed description of the issuer's project, the type of crypto-asset that will be offered to the public or for which admission to trading is sought, the reasons why the crypto-assets will be offered to the public or why admission to trading is sought and the planned use of the fiat currency or other crypto-assets collected via the offer to the public;
- (c) a detailed description of the characteristics of the offer to the public, in particular the number of crypto-assets that will be issued or for which admission to trading is sought, the issue price of the crypto-assets and the subscription terms and conditions;
- (d) a detailed description of the rights and obligations attached to the crypto-assets and the procedures and conditions for exercising those rights;
- (e) information on the underlying technology and standards applied by the issuer of the crypto-assets allowing for the holding, storing and transfer of those crypto-assets;
- (f) a detailed description of the risks relating to the issuer of the crypto-assets, the crypto-assets, the offer to the public of the crypto-asset and the implementation of the project;
- (g) the disclosure items specified in Annex I.

Additionally, the whitepaper must include the following statement: ***'The issuer of the crypto-assets is solely responsible for the content of this crypto-asset whitepaper. This crypto-asset whitepaper has not been reviewed or approved by any competent authority in any Member State of the European Union'***.

The whitepaper also needs to include a **summary** which should read as an introduction to the whitepaper and include a number of required statements such as a confirmation that the whitepaper is not a prospectus and that the tokens issued are not financial instruments.

Every whitepaper **must be dated**. It must also include a **statement from the management body of the issuer of the crypto-assets confirming that the whitepaper complies with the requirements of this title**, specifying that, to best of their knowledge, the information presented in the document is correct and **that there are no significant omissions** making the whitepaper misleading.

The whitepaper must be written in **at least one of the official languages** of the home Member State or in a language customary in the sphere of international finance.

The whitepaper must be made available in **machine-readable formats**. ESMA will develop technical standards to establish standard forms, formats and templates for the production of machine-readable whitepapers.

Marketing

Rules for marketing include that:

- (a) marketing communications are **clearly identifiable as such**;
- (b) the information is **fair, clear, and not misleading**;
- (c) the information contained in the marketing communications **is consistent with the information in the whitepaper**;
- (d) the marketing communications **clearly state that a whitepaper has been published** and indicate the **address of the website of the issuer** of the crypto-assets concerned.

Notification requirements

Article 7 covers the **notification requirements to the regulator**, which include that:

- Regulators will not be required to approve a whitepaper or any marketing communications. However, the whitepaper will **need to be notified twenty working days before publication**.
- An assessment must be provided explaining the reasons why the crypto-asset described in the whitepaper **is not a financial instrument or other type of asset regulated under other EU legislation**.
- The issuer will also **inform the regulator** of issuances planned in **other Member States**, as well as any planned **listings on a trading platform** which is **not in its home Member State**. The regulator will then need to **inform the other EU regulators** where issuances or listings are planned within **two working days**.

Publication

Issuers must publish all whitepapers on their website **no later than the starting date of the offering or admission to trading**. The published whitepaper must **remain available on the issuer's website** for as long as the crypto-assets are held by the public and be **identical to the version notified** to the relevant regulator.

Upon publication of a MiCA-compliant whitepaper, the issuer can offer those crypto-assets (except for asset-referenced tokens or e-money tokens) **to the entire union** and **seek admission to a trading platform** for crypto-assets without being subject to further information requirements. Where a time limit is set on the public offering of crypto-assets, issuers must publish the results of the offering within 16 working days from the end of the subscription period.

Modifications

Article 11 outlines the rules to modify the whitepaper (and, where applicable, promotional materials) following their publication.

Right of withdrawal

- a) Issuers of crypto-assets must offer a **right of withdrawal** to consumers which purchase these crypto-assets either directly from the issuer or from a CASP selling the crypto-assets on behalf of the issuer. Consumers **may exercise this right to withdraw their crypto-asset purchase agreement without incurring costs or giving reasons up to 14 days after their purchase**. Information relating to this right must be included in the crypto-asset whitepaper.
- b) The relevant **issuer or CASP** must **reimburse all payments** received by the consumer without undue delay and **no later than 14 days after being informed** of the consumer's withdrawal decision.
- c) The right of withdrawal **does not apply** where the crypto-assets are admitted to a trading platform and may not be exercised after the end of a public offering's subscription period.

Currently, very few token issuances offer a right of withdrawal. Unless programmed into a smart contract which would allow customers to withdraw with little to no input by the issuer, this will require the implementation of procedures into the issuance process to allow for this right to be exercised.

Liability

Holders of crypto-assets may **claim damages** from an issuer or its management body for **breaches of requirements under Article 5** to provide detailed information in the whitepaper that is fair, clear, complete, and not misleading.

Title III: Asset-referenced tokens

There are several common requirements for the issuance of **asset-referenced tokens** to those applicable to the **issuance of crypto-assets**, however, some key differences apply. Notably, issuers of asset-referenced tokens must be **authorised by the designated regulator** in their home Member State prior to being allowed to offer tokens to the public or to seek admission of these tokens to trading on a trading platform. In order to obtain authorisation, issuers of asset-referenced tokens must be **established as a legal entity in the EU**.

There are three exemptions to the requirement to be authorised: 1) **credit institutions** that issue asset-referenced tokens; and, in respect of a specific issuance, where the outstanding asset-referenced tokens are 2) **below EUR 5,000,000** or 3) **are issued to qualified investors**. Despite these exemptions, **publication of a whitepaper is always required**.

Entities authorised in a Member State will benefit from the right to passport, which means that their authorisation will be valid across the Union.

Article 16: Application for authorisation

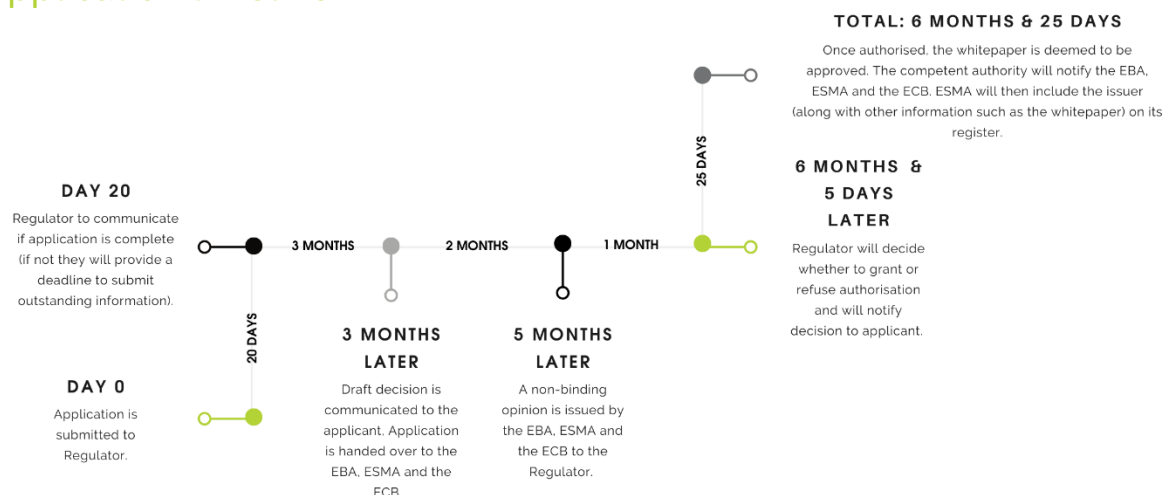
When seeking authorisation as issuers of asset-referenced tokens, these entities must submit an **application** to the relevant regulator in their home Member State. The application pack must include a set of defined information including, for example; **a business plan**, **a legal opinion confirming that the asset-referenced tokens do not qualify as financial instruments, e-money, deposits, or structured deposits**, a detailed description of the governance structure, and the whitepaper.

Crypto-asset whitepaper for asset-referenced tokens

In addition to the information required under Article 4, whitepapers for asset-referenced tokens must also include the information specified in Article 17. This includes information relating to the governance arrangements, the reserve of assets, the custody arrangements, the investment policy, rights of token holders, and complaints handling procedures.

Where no direct claim or redemption right has been granted to all the holders of asset-referenced tokens, the crypto-asset whitepaper needs to contain **a clear and unambiguous statement that all the holders of the crypto- assets do not have a claim on the reserve assets, or cannot redeem those reserve assets with the issuer at any time**.

Application timeline



Obligations of all issuers of asset-referenced tokens

Asset-referenced token issuers will have to comply with **obligations similar to those for crypto-asset issuers under Title II**. These are set out under chapter 2 of this title and include, for example, the obligation to act **honestly, fairly and professionally** in the best interest token holders, to comply with defined requirements on **marketing communications** and **complaint handling procedures**, and to have policies in place regarding **conflicts of interest**.

Article 26: Ongoing information

Issuers of asset-referenced tokens are required to provide certain information on an ongoing basis. For instance, the need to disclose on their website, on a monthly basis, the **number of asset-referenced tokens in circulation** and the **value and composition of the reserve assets**.

They are also required to disclose the **outcome of the audit of reserve assets**, which must be conducted every six months.

Currently, few stablecoin issuers make such public disclosures of reserves. Although the increased transparency will be welcomed by the industry, this will present an operational challenge for these firms. The audit of reserve assets will present another challenge, as there are currently few audit firms which specialise in the audit of such assets. As such, the cost of these audits will make it difficult for smaller players to achieve and maintain compliance.

Article 30: Governance arrangements

The management body of issuers of asset-referenced tokens must be fit and proper, which means that all members must be of good repute and must have the appropriate level of knowledge, skills, experience and, for certain positions, be suitably qualified to perform their duties.

Issuers are also required to **maintain policies and procedures** that are sufficiently effective to ensure compliance with MiCA. These policies and procedures relate to, for example, the **reserve assets and their custody**, the **rights or absence of rights** granted to holders, the **mechanism through which the tokens are issued, created, and destroyed**, and the **protocols for validating transactions** and **business continuity**.

In addition, issuers of asset-referenced tokens will have to implement systems and internal control mechanisms for security access protocols, risk assessment and management, data protection, and must be regularly audited by an independent auditor.

Article 31: Own funds requirements

Issuers of asset-referenced tokens must, at all times, have in place own funds equal to an amount of at least **the higher** of the following:

- a) **EUR 350 000**;
- b) **2% of the average amount of the reserve assets** referred to in Article 32.

For the purpose of point (b), the average amount of the reserve assets shall mean **the average amount of the reserve assets at the end of each calendar day, calculated over the preceding 6 months**.

The own funds shall consist of the **Common Equity Tier 1 items and instruments referred to in Articles 26 to 30 of the Capital Requirements Regulation (575/2013)**.

Regulators of issuers of asset-referenced tokens may require them to hold an amount of own funds up to 20% higher or 20% lower than the amount resulting from the application of paragraph 1, point (b).

These capital requirements will make it difficult for smaller players to establish themselves as issuers of asset-referenced tokens. On the other hand, prudential requirements will enhance consumer protection as issuers will be better funded.

Reserve of assets

Asset-referenced token issuers are required to **create and maintain a reserve of assets**.

The management body is required to manage the reserves prudently, ensuring that the creation and destruction of asset-referenced tokens is matched by an increase or decrease in the reserve of assets.

The issuer must have a **clear and detailed policy covering the stabilisation mechanism**, including how the asset-referenced token will be stabilised relative to the referenced assets through the **management of the reserve**. The method through which the tokens are created and destroyed, and their interaction with the reserve, must also be clearly set out.

From the date of authorisation, an independent audit of the reserve assets must be conducted every six months.

Article 33: Custody of reserve assets

Rules around the **custody of reserve assets** are broad and require that suitable policies, procedures, and contractual arrangements are established to ensure that the reserve assets are:

- a) **segregated** from the issuers' own assets;
- b) not **encumbered nor pledged** as a 'financial collateral arrangement', a 'title transfer financial collateral arrangement' or as a 'security financial collateral arrangement';
- c) **held in custody**;
- d) **promptly accessible** to meet any redemption requests.

An issuer is required to produce a **separate custody policy for each reserve of assets in respect of every issuance**.

Reserve assets received in exchange for the asset-referenced tokens are required to be **held in custody no later than 5 business days after the issuance of the asset-referenced tokens** by either:

- a) **a crypto-asset service provider authorised** under Article 53, where the reserve assets take the form of crypto-assets;
- b) **a credit institution for all other types of reserve assets.**

This will be challenging for current providers that rely on crypto-assets to stabilise the token price relative to a reference asset. Assets such as DAI are stabilised by locking Ethereum in a smart contract in a collateralised debt position (CDP). A project such as this could require the assets to be stored by a third party – fundamentally changing the proposition.

Article 34: Investment of the reserve assets

Reserve assets must only be invested in **highly liquid financial instruments** with **minimal market and credit risk** and must be capable of being **liquidated rapidly with minimal adverse price effects**.

All profits or losses, **including fluctuations in the value of the financial instruments** and any counterparty or operational risks that result from the investment of the reserve assets, are required to be borne by the issuer.

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

Issuers of asset-referenced tokens must clearly communicate the redemption rights granted to token holders. Policies and procedures must be in place in respect of tokens granting a **direct claim** on the issuer, including conditions, thresholds, periods, and timeframes for users to exercise rights, redemption mechanisms, valuation methodologies, and fees.

Where the issuer **does not grant redemption rights**, it will need to put in **place mechanisms to ensure the liquidity of asset-referenced tokens**. The issuer will need to ensure that a sufficient number of CASPs post firm quotes at competitive prices on a regular and predictable basis.

The issuer must also establish and maintain **contractual arrangements** to ensure that **the proceeds of the reserve assets** are paid to the holders of asset-referenced tokens where the issuer a) decides to **stop operating**; b) has been placed under an orderly **wind-down**; or c) has its **authorisation withdrawn**.

Article 36: Prohibition of interest

Issuers of asset-referenced tokens or CASPs **shall not provide for interest or any other benefit** related to the length of time during which a holder of asset-referenced tokens holds asset-referenced assets.

Article 39: Classification of asset-referenced tokens as significant

Asset-referenced tokens which meet at least three of the following criteria will be deemed significant at the point of authorisation, and will be re-assessed by regulators yearly:

(a) the size of the customer base exceeds two million natural or legal persons;

(b) the value of the asset-referenced tokens issued or, where applicable, their market capitalisation exceeds EUR 1 billion;

(c) the number and value of transactions in those asset-referenced tokens exceeds 500,000 transactions per day or EUR 100 million per day;

(d) the size of the reserve of assets of the issuer of the asset-referenced tokens exceeds EUR 1 billion;

(e) the asset-referenced token is used in seven or more Member States.

The EBA will also assess whether the issuer of asset-referenced tokens is significant, in which case their supervision will be carried out by the EBA.

Article 41: Specific additional obligations for issuers of significant asset-referenced tokens

Requirements for issuers of significant asset-referenced tokens will be more onerous than for non-significant token issuers given that the associated risks are significantly higher. Specific requirements for these types of issuers include:

A remuneration policy that promotes sound and effective risk management and that does not create incentives to relax risk standards.

Ensure that tokens can be held in custody by different CASPs, including by CASPs not part of the same group, on a fair, reasonable and non-discriminatory basis.

Establish a liquidity management policy and procedures.

Capital requirement threshold shall be set at **3% of the average amount of the reserve assets** for issuers of significant asset-referenced tokens, **rather than 2%** for those which are not significant.

Orderly wind-down

Issuers of asset-referenced tokens are required to **implement a wind-down plan**. This will be used to demonstrate the ability of the issuer to **carry out an orderly wind-down** without causing **undue economic harm** to token holders or the **stability of markets** of the reserve assets.

The plan will include **contractual arrangements, procedures and systems** to ensure the proceeds from the sale of the reserve assets are **paid to the token holders**.

Title IV: Electronic money tokens

Electronic money tokens or e-money tokens are defined as a type of 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**. Issuers of such tokens will have to comply with three primary requirements:



To be authorised as a bank or an e-money institution.



To comply with the requirements applicable to e-money institutions set out in Titles I & II of the E-Money Directive (2009/110/EC).



To publish a white paper notified to its Regulator in accordance with Article 46.

There are some **exemptions** for e-money tokens that are only marketed, distributed and held by qualified investors, where the average amount of outstanding e-money tokens is below the threshold of EUR 5,000,000 over a 12-month period, or below the lower threshold set by the issuer's Member State.

Issuance and redeemability

The requirements of this title oblige issuers of e-money tokens to:

- provide e-money token holders with a **claim on the issuer**;
- issue e-money tokens **at par value** on receipt of funds;
- redeem, upon request of the holder, **at any moment and at par value**, the monetary value of the tokens held either **in cash or by credit transfer**;
- **state the conditions of redemption prominently in the whitepaper**, including any applicable fees. Redemption fees may only be applied where these have been clearly stated in the whitepaper and must be proportionate and commensurate with the actual costs incurred.

Article 45: Prohibition of interests

As with asset-referenced tokens, issuers of e-money tokens or CASPs **shall not provide for interest or any other benefit** related to the length of time during which a holder of e-money tokens holds these tokens.

Article 46: Content and form of the crypto-asset whitepaper for electronic money tokens

The required **content and form of the whitepaper** for e-money tokens is similar to that required under **Title II** for crypto-asset issuances.

The whitepaper must:

- be **published on the issuer's website**, including the information required under Title II and published in the same format;
- be **fair, clear and not misleading**, without any **material omissions**;
- include a statement **confirming compliance** with Title IV;
- include a **summary** which confirms that the token holders have a **redemption right at any moment and at par value**, and explains the redemption **conditions and fees**;
- have **modification provisions** when there are changes which will have a significant influence on the decision of a potential purchaser.

Liability of issuers

As with issuance of crypto-assets and asset-referenced tokens in Title II and Title III, there are provisions to give holders of e-money tokens the opportunity to **claim for damages** when there is an infringement of Article 46.

Marketing communications

Marketing communications are to be drawn up on the same basis as other issuances, with the additional requirement to contain a **clear and unambiguous statement** that all **holders of the e-money tokens have a redemption right at any time and at par value on the issuer**.

Investment of funds received in exchange of e-money token issuers

Funds received by issuers of e-money tokens in exchange of e-money tokens and that are **invested in secure, low-risk assets** in accordance with Article 7(2) of Directive 2009/110/EC must be **invested in assets denominated in the same currency** as the one referenced by the e-money token.

Significant e-money tokens

The EBA shall classify e-money tokens as **significant e-money tokens** using the **same criteria and on the same basis** used to classify significant asset-referenced tokens, and where at least **three** of the criteria set out in Title III are met. Where the token is considered significant, the EBA will be the designated regulator of the issuer.

Additional obligations

Issuers of at least **one category of e-money tokens** shall apply the following requirements which apply to issuers of asset-referenced tokens and significant asset-referenced tokens:

- a) Articles 33 and 34 of MiCA (**covering custody and investment of the reserve assets**) instead of Article 7 of Directive 2009/110/EC;
- b) Paragraphs 1, 2 and 3 of Article 41 of MiCA, which bring in similar **additional provisions** as with significant asset-stabilised tokens, such as **liquidity management**, and the **ability for the tokens to be held in custody and by CASPs outside the issuers' group**;
- c) Paragraph 4 of Article 41 of MiCA, instead of Article 5 of Directive 2009/110/EC, being the **3% of the average amount of reserve assets** as the higher of its capital requirements;
- d) Article 42 of MiCA, requiring a **wind-down plan**.

Title V: Authorisation and operating conditions for Crypto-asset Service Providers

Any person providing, by way of business, any of the services defined in this Regulation as crypto-asset services, will be **categorised as a CASP** and will need to be **authorised as such to operate**.

CASPs seeking authorisation in the EU will need to demonstrate to their relevant regulator that they have sufficient capital to prudently operate and to absorb losses; that they have effective governance arrangements and internal control systems; that they will act in their clients' best interests; and that they have systems in place to detect and prevent market abuse and market manipulation.

Authorisation of crypto-asset service providers

Only **legal persons with registered offices** in an EU Member State will be eligible to apply for **authorisation as a CASP**.

As is currently the case with other types of financial services governed by European Directives and Regulations, MiCA will introduce '**passporting**' rights, which will allow **CASPs authorised in one Member State to provide crypto-asset services throughout the EU**, either by establishing a branch or some other form of physical presence, or on a services basis (i.e. remotely). CASPs looking to provide cross border services would need to **notify their regulator**.

ESMA will be required to **maintain a public register of all CASPs authorised in the EU**.

Legal persons seeking **authorisation as a CASP** will need to **submit an application** to the regulator in the Member State where they have their registered office. Article 54 of the Regulation provides a comprehensive list of the information that will need to be submitted as part of the application. The information required will include details of the legal entity, information on its policies and procedures, and its proposed programme of operations, including governance arrangements, risk management, and a business continuity plan.

Any CASP **already operating** in a Member State under an existing national crypto-asset regime will not be required to resubmit any of the above information, as long as any information provided at the time of its authorisation is still up to date.

To provide payment services related to the crypto-asset services they offer, CASPs must also be authorised as a payment institution.

Regulators may refuse authorisation if they believe that authorising a CASP would pose a risk to consumers or the integrity of the market.

Application timeline



Prudential requirements

CASPs will need to **maintain sufficient capital** to meet their prudential requirements. At all times, they will need to have funds equal to or higher than either of the following:

- the minimum capital requirement prescribed in Annex IV (at the time of writing, Annex IV has not yet been published) of the Regulations, according to the crypto-asset services provided;
- **one quarter of the fixed overheads of the previous year**, to be reviewed annually.

Although this will undoubtedly increase the cost and amount of capital needed to provide crypto-asset services across the EU, firms will become more resilient to market downturns and economic crises.








Additional requirements

Other requirements with which CASPs will need to comply include having in place procedures to handle **complaints** and manage **conflicts of interest**, as well as **provisions for outsourcing of certain activities**.

Organisational requirements

CASPs seeking authorisation in the EU will need to demonstrate to the regulator that their management body is **fit and proper** and that, collectively, they have an **appropriate level of knowledge, skills and experience** to perform their duties and comply with their regulatory obligations. Beneficial owners that own, directly or indirectly, more than 20% of the share capital or voting rights, or who exercise control of the CASP, will also need to demonstrate that they are fit and proper.

In order to obtain authorisation, all CASPs must demonstrate that they meet the following organisational requirements:

 <p>Employ personnel with the skills, knowledge and expertise necessary to discharge their responsibilities.</p>	 <p>Ensure continuity and regularity in the delivery of services to clients.</p>	 <p>Establish an effective business continuity policy and disaster recovery plans.</p>
 <p>Have internal control mechanisms and effective procedures for risk assessment.</p>	 <p>Have systems and procedures to safeguard the security, integrity and confidentiality of information held.</p>	 <p>Keep records of all crypto-asset services, orders and transactions undertaken.</p>
 <p>Have systems and procedures in place to monitor and detect market abuse and be able to immediately report any suspicion to their regulator.</p>		

Safekeeping of clients' crypto-assets and funds

A CASP that is authorised to hold or access crypto-assets or fiat funds belonging to clients will need to **demonstrate it can safeguard** the ownership rights of clients, especially in the event of insolvency.

Fiat funds belonging to clients will need to be held **separately from the CASPs own funds**, either with a central bank or a credit institution.

Obligations for the provision of specific crypto-asset services

In addition to the general requirements that will apply to all CASPs, MiCA will introduce provisions that will apply depending on the crypto-asset services provided, designed to address risks inherent in the nature of certain activities. The specific requirements for each defined service are set out in the following sections.

Custody on behalf of third parties of crypto-assets or access to crypto-assets

CASPs that provide **crypto-asset custody services** will need to demonstrate that they comply with the provisions set out in Article 67, designed to **minimise the risk of loss** of those assets.

They will need to have a **contract in place** with each client which clearly sets out the service being offered, the security system in place to protect the crypto-assets, and the fees and responsibilities of the CASP. CASPs will need to have a **custody policy** in place aimed at ensuring the safekeeping of the crypto-assets and maintain a register of all client positions.

The regulations require **CASPs to keep any crypto-assets held in custody separate from their own holdings**.

CASPs will be held liable for any losses resulting from malfunctions or hacks, up to the market value of the crypto-assets lost.

Operation of a trading platform for crypto-assets

CASPs authorised **to operate a trading platform** will need to comply with the requirements set out in Article 68 and establish operating rules. The operating rules include **minimum due diligence and approval processes for admittance of crypto-assets**, policies and procedures regarding fees and liquidity, and requirements to ensure fair and orderly trading.

CASPs will be responsible for ensuring that **all listings comply with operating rules**, and that no crypto-asset should be admitted unless it has published **a whitepaper in line with this Regulation**.

All tokens listed on EU trading platforms are required to provide whitepapers which are compliant with MiCA – it is difficult to imagine how this would be possible for decentralised crypto-assets.

No crypto-assets which have inherent anonymisation functions (such as ‘privacy coins’) can be admitted onto a trading platform unless the holders of the crypto-assets and their transaction history can be identified by the CASP or the relevant regulator.

This may prove almost impossible to comply with and could result in most EU crypto-asset exchanges delisting privacy coins.

Fee structures must be transparent, fair and non-discriminatory, and not create incentives that could lead to disorderly trading conditions or market abuse.

CASPs will need to ensure that their trading systems are resilient and have the capacity to operate under severe market stress.

Exchange of crypto-assets against fiat currency or exchange of crypto-assets against other crypto-assets

CASPs authorised to exchange crypto-assets against fiat currency or other crypto-assets will need to establish a **non-discriminatory commercial policy** that indicates the type of clients they accept and the conditions that must be met by clients. They must publish a firm price for any crypto-assets exchanged or the method used to determine the price such crypto-assets.

Execution of orders for crypto-assets on behalf of third parties

CASPs authorised to execute orders for crypto-assets must ensure that they **secure the best possible result for their clients** taking into account best execution factors such as price, cost and speed, unless following explicit client instructions.

An **order execution policy** which seeks to prevent the misuse by employees of any information relating to client orders must be established.

Reception and transmission of orders on behalf of third parties

Requirements for CASPs authorised to provide **reception and transmission of orders** include requirements to implement procedures and arrangements to ensure the prompt and proper transmission of clients' orders. Also, **CASPs must not receive any remuneration or other incentive for routing orders received from clients to a particular trading platform or to another CASP**. In addition, they must not misuse any information held relating to pending clients' orders and must take reasonable steps to prevent the misuse of such information by any of their employees.

Advice on crypto-assets

CASPs providing **advice must assess the compatibility of crypto-assets with the needs of their clients** and make recommendations only when this is in the interest of the client.

Similar to requirements for **traditional investment advisors**, CASPs will need to have in place policies and procedures requiring them to gather information about their clients' knowledge and experience in crypto-assets, investment objectives and financial situation, including the ability to bear losses and their understanding of the risks involved.

If a CASP determines that a **client has insufficient knowledge, they must issue a risk warning and provide advice suggesting that crypto-assets might be inappropriate for them**. That risk warning must clearly state the risk of losing the entirety of the money invested, and clients have to expressly acknowledge that they have received and understood the warning.

Title VI: Prevention of Market Abuse involving crypto-assets

Rules concerning **market abuse** apply to any **activity conducted by any person in relation to crypto-assets admitted to trading on a trading platform operated by an authorised CASP**, or for which a request to trading on such a trading platform has been made.

This title covers the **requirement to disclose inside information** to the public and sets out the following offences: unlawful disclosure of inside information, insider dealing, and market manipulation.

Article 77: Disclosure of inside information / Article 79: Prohibition of unlawful disclosure of inside information

Inside information is information of a precise nature that has not been made public, which relates, directly or indirectly, to one or more crypto-asset issuers or crypto-assets. If made public, it would be likely to **significantly impact the prices of those crypto-assets**. A crypto-asset issuer is required to inform the public of inside information as soon as possible, ensuring that the information **reaches as many people as possible** and allows for complete, correct and timely assessment by the public.

Crypto-asset issuers may, however, delay the disclosure of inside information in certain circumstances.

Article 79 prohibits the unlawful disclosure of inside information. Inside information can only be disclosed in the normal exercise of an employment, a profession, or duties.

Article 78: Prohibition of insider dealing

Insider dealing takes place when a person possesses inside information and uses it by acquiring or disposing of crypto-assets to which the information relates. This may be done for the person's own account or that of a third party, directly or indirectly. Recommending or inducing another person to engage in insider dealing is prohibited in the same way as insider dealing.

Article 80: Prohibition of market manipulation

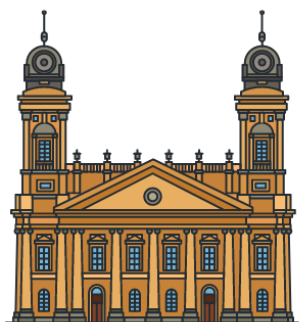
Market manipulation comprises:

- a) entering into a transaction, placing an order to trade, or any other behaviour which, unless carried out for legitimate reasons:
 - i. gives or is likely to give false or misleading signals as to the price, supply or demand of/for a crypto-asset.
 - ii. sets or is likely to set the price of one or several crypto-assets at an abnormal or artificial level.
- b) entering into a transaction, placing an order to trade, or any other behaviour which affects or is likely to affect the price of one or several crypto-assets, which employs a fictitious device or any other form of deception or contrivance;
- c) disseminating information through the media, or any other means which gives or is likely to give false or misleading signals as to the price, supply, or demand of/for a crypto-asset or is likely to secure the price of one or more crypto-assets at an abnormal or artificial level, including the dissemination of rumours, where the person disseminating the information knew or ought to have known that it was false or misleading.

Title VII: Competent Authorities, the EBA and ESMA

This title is split in four chapters setting out the **powers that regulators, the EBA and ESMA must have**, the obligation to **cooperate and exchange information** between authorities, the administrative **measures and sanctions** available to regulators, and the **supervisory responsibilities, powers and competencies** of the EBA regarding issuers of significant tokens, including details on the requirements to establish supervisory colleges.

Member states shall:



- Designate the competent authorities responsible for carrying out the functions and duties under MiCA.
- When more than one, their respective tasks must be determined and one must be designated as the single point of contact for cross-border administrative cooperation between competent authorities, ESMA, and the EBA.
- A list of all designated competent authorities will be published on ESMA's website.

Powers of competent authorities must include:

to require information and documentation
to suspend or prohibit activities or offers, including to order the immediate cessation of activities
to disclose or require disclosure of all material information
to make failures to comply with obligations public
to transfer existing contracts to another service provider
to take appropriate administrative measures and sanctions in relation to a minimum set of infringements
to carry out onsite inspections or investigations

Cooperation between competent authorities

Regulators must **cooperate and exchange information** with each other, with authorities in other Member States and third countries, and with the EBA and ESMA.

ESMA will develop regulatory technical standards to specify the information to be exchanged and implementing technical standards to establish standard forms, templates and procedures for the cooperation and exchange of information.

Complaint handling by competent authorities

Regulators must have **complaint handling procedures** in place for complaints to be submitted regarding alleged infringements of MiCA by issuers and CASPs. Information on the procedure should be published on the regulator's website and communicated to the EBA and ESMA.

Administrative measures and sanctions

Regulators must have the **power to take appropriate administrative measures** and sanctions when MiCA is infringed. These measures and sanctions include public statements of the infringement(s), orders to cease conduct, and administrative pecuniary sanctions.

Aggregate information on all administrative measures and penalties shall be reported to ESMA and the EBA annually.

Title VIII: Delegated acts and implementing acts

Under Article 109 of MiCA, the **European Commission has the power to adopt delegated acts which amend or supplement MiCA**, though the European Parliament or the Council may withdraw the delegation of powers or object to certain delegated acts to block their adoption.

Title IX: Transitional and final provision

Within 36 months of MiCA entering into force, the Commission will consult the EBA and ESMA before providing a report to the European Parliament and Council on the application of MiCA. This report will assess a range of areas including, most notably, the following:

- a) number of **crypto-assets issued** and **whitepapers registered** in the EU;
- b) levels of **fraud, hacks and theft** of crypto-assets in the EU, and the number and nature of **complaints** made to CASPs and regulators;
- c) number of **authorised issuers of asset-referenced tokens and e-money tokens**, with evaluation of their **reserves** of assets and **transaction volumes**;
- d) level of **consumer protection, market integrity** and **financial stability** provided by MiCA, and whether amendments to MiCA are necessary to achieve these objectives;
- e) whether the **scope, definitions** and **exemptions** under MiCA require amendment.

Following MiCA's entry into force, there will be an 18-month transitional period during which various measures will facilitate the transition to compliance with MiCA. For example, during this period, MiCA will only apply to e-money tokens, asset-referenced tokens, and their issuers, and CASPs may continue to provide crypto-asset services within the scope of MiCA as long as they comply with national law.

Conclusion

The publication of MiCA marks a seminal moment for crypto-assets. MiCA's scope is all-encompassing. It will have profound and wide-reaching implications for everyone involved with crypto-assets and related services, both in the EEA and across the world. Other jurisdictions may well use MiCA as a template for their own crypto-asset regimes, although some may choose to differentiate themselves in order to obtain a competitive advantage.

MiCA aims to bring much-needed legal and regulatory certainty to the crypto-asset industry to support innovation, provide consumer and investor protection, and ensure financial stability. The Regulation leaves no stone unturned. All crypto-assets and crypto-asset services will be caught by the new legislation, including existing coins and tokens.

MiCA will also present significant challenges for an industry in which many activities have, until now, been unregulated. As such, the role of ESMA and the EBA in supporting MiCA compliance through publication of technical standards and guidance will be key. However, it remains to be seen how the Regulation will co-exist with innovative decentralised projects which may prove difficult to subject to regulatory requirements.

Significant resources will be needed to comply with MiCA, by both regulators and regulated. Issuers and CASPs operating in the EEA or with EEA clients should consider the strategic implications brought about by MiCA and begin planning accordingly. The clock is now ticking on the legislative process and so time is short in which to make representations. To do this, however, businesses first need to understand the implications of this new crypto-asset law on their activities

XReg is a team of policy and regulatory experts, based in Gibraltar, Brussels and London, dedicated to assist governments, regulators, public bodies and the private sector in dealing with the challenges of continuously evolving crypto-asset regulation. If you would like to discuss anything mentioned in this document or otherwise related to MiCA, feel free to contact Siân Jones, Ernest Lima or Ana James:



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