

CLIENT ALERT

How the MiCA Regulation Will Impact the Crypto-Asset Market in Europe and Beyond

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Introduction

It has almost been two years since the European Commission published its first draft of a Markets in Crypto Assets Regulation (**MiCA**). On June 30, 2022, after three months of trilogue negotiations between the European Parliament, the Council and the European Commission, a compromise was reached and a final text for MiCA appears to be agreed upon, albeit not published yet.

MiCA will introduce a comprehensive legal framework harmonizing the regulatory requirements for crypto-asset-related services across Europe. More specifically, its intention is to lay down uniform rules for:

- The issuance and trading of crypto-assets;
- The authorization and supervision of crypto-asset services providers and issuers of asset-referenced and e-money tokens;
- Consumer protection for the issuance, trading, exchange and custody of crypto-assets; and
- The prevention of market-abuse and ensuring the integrity of crypto markets.

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This briefing provides an overview over the key concepts of MiCA. Since the final text is not published yet and still needs to undergo the formal legislative process of the EU, changes cannot be excluded. We have commented on aspects of particular uncertainty.

Scope

To determine whether a business activity will be subject to MiCA rules, a number of factors need to be taken into account: What types of assets are concerned, what is the exact activity an undertaking or a person carries out and where is this service deemed to be located?

In-scope assets

The core subject matter of MiCA is the **crypto-asset**, which MiCA defines as “a digital representation of value or rights which may be transferred and stored electronically, using technology that support the distributed recording of encrypted data (DLT) or similar technology”.

Reflecting actual use cases for stable coins, MiCA comes with dedicated sub-sets of rules for specific types of crypto-assets. While the definitions of crypto-asset types were all subject to debate as part of the trilogue, the below categories reflect likely definitions based on the latest draft documents published in connection with the trilogue negotiations.

- **Asset-referenced token** will likely be defined as a type of crypto-asset that is not an electronic money token and that purports to maintain a stable value by referring to any other value or right or combination thereof, including one or several official currencies of a country. This can include algorithmic stable coins.
- **Electronic money token** will likely be defined as a type of crypto-asset the main purpose of which is to be used as a means of payment and that purports to maintain a stable value by referring to the value of only one official currency of a country. While only the electronic money token definition requires payment to be the main purpose, this does not mean that asset-referenced tokens cannot be used as a means of payment. It may well be that the criterion will be removed in the final draft. If so, the question will arise of how asset-referenced tokens are distinguished from electronic money tokens. The Commission’s concern about referencing currencies of countries was that the high regulatory requirements for the issuance of e-money could be circumvented by issuing e-money token.
- Finally, **utility token** will likely be defined as a type of fungible crypto-asset which is only intended to provide access to a good or service, by the issuer of that token and is not an asset-referenced token or an e-money token.

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Crypto-assets under MiCA			
Asset-referenced tokens ("stable coins")	Electronic money tokens ("crypto currencies")	Utility tokens	All other crypto-assets
Significant asset-referenced tokens	Significant electronic money tokens		

Non-fungible tokens (NFTs), i.e., digital assets representing real objects like art, music and videos, are excluded from the scope, unless they fall under the above crypto-asset categories. However, the European Commission is tasked to prepare a comprehensive assessment as to the necessity to create a bespoke regime for NFTs.

In-scope activities and persons

MiCA applies to all persons who are engaged in one of the following main categories of regulated activities covered by MiCA:

- Issuance/offering of crypto-assets; and
- Crypto-asset service providers (CASP)

The most relevant exemptions that the original draft provided for concern undertakings which are already subject to financial regulatory supervision:¹

- **Credit institutions** authorized under Directive 2013/36/EU are exempt from authorization requirements when issuing asset-referenced tokens and providing crypto-asset services. At the same time, besides e-money institutions, they are the only eligible issuers for electronic money token.
- **Investment firms** authorized under Directive 2014/65/EU (MiFID) are also exempt from the authorization requirement for a crypto-asset service if they are already authorized for an equivalent investment service under MiFID.

¹ It is not yet clear whether these exemptions will be included in the final version of MiCA.

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The below table shows the equivalent MiFID services pursuant to Art. 2 (6) MiCA:

Crypto-asset Service (MiCA)	Equivalent Investment Service (MiFID)
Operation of a trading platform for crypto-assets	Operation of an MTF
Exchange of crypto-assets for fiat currency and exchange of crypto-assets for other crypto-assets	Dealing on own account
Execution of orders for crypto-assets on behalf of third parties	Execution of orders on behalf of clients
Placing of crypto-assets	Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis and Placing of financial instruments without a firm commitment basis
Reception and transmission of orders for crypt- assets	Reception and transmission of orders in relation to one or more financial instruments
Advice on crypto-assets	Investment advice
Portfolio management	To be confirmed. ²

MiCA is silent on **AIFMs** with a so-called **MiFID top-up licenses**. The draft of the exemption only refers to investment firms authorized under MiFID. Since the exemption refers to investment firms authorized under MiFID, it seems it will not apply to AIFMs or UCITS management companies with top-up licenses. Where AIFMs manage funds which acquire crypto-assets, the rules of MiCA do not apply.

² The trilogue documentation did not cover this point, since portfolio management was not provided in the original draft.

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Territorial scope

The territorial scope of MiCA is determined by the activities covered by MiCA, i.e., the rules apply if crypto-assets are offered to the public, admitted to trading on a trading platform for crypto-assets or where crypto-asset services are provided in the EU. However, the authorization requirements attached to the issuance of asset-referenced tokens, electronic money tokens and the provision of crypto-asset services will require an establishment in the EU, effectively excluding third-country entities from these activities.

General rules for issuers of crypto-assets

The offering and admission to trading on a trading platform for crypto-assets is subject to certain procedural and conduct rules:

- The offering shall only be made by a legal person;
- The creation of a white paper in accordance with an annex supplementing MiCA covering information on the issuer, the project and the offer of crypto-assets;
- The notification of that white paper and all marketing communications, if any, to the competent authority at least 20 days prior to its publication;
- The publication of the white paper no later than the day the offering commences; and
- The compliance with certain good conduct and organizational requirements.

These requirements will not apply where the crypto-assets are offered only to qualified investors, which are defined to include eligible counterparties as well as professional clients as defined under MiFID. In addition, certain de minimis exemptions will apply where the amount of the offer does not exceed certain thresholds.

Specific rules for stable coins in the form of asset-referenced tokens (ART)

MiCA introduces increased regulatory requirements applicable to the issuance and the offering of asset-referenced token (ART):

- The issuance of ART will require an **authorization**. The information which needs to be submitted as part of the authorization procedure will be set out in regulatory technical standards to be developed by the EBA in cooperation with ESMA. Taking into account the procedural steps in order to obtain an authorization to issue an ART, the timeframe for such authorization is likely to be in the range of a seven to eight months of minimal processing period, which does not include the preparation of the application.

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- One key element of ART is the constitution and maintenance of an **asset reserve**. While the concept was subject to debate during the trilogue negotiations, it now appears that the reserve will serve to underlie a mandatory redemption right which issuers of ART must grant to token holders. The investment of the asset reserve must follow a defined policy ensuring sufficient liquidity of the reserve. Furthermore, comprehensive mandatory custody rules apply to the asset reserve which are comparable to custody rules applicable to assets belonging to funds. Whether the original proposal that such redemption rights can be replaced by a compensatory appointment of one or more market makers will stay in place appears less likely.
- Issuers of ART will be subject to **own funds requirements** of at least EUR 350,000 or 2% of the reserve assets.
- Issuers of ART will be subject to a comprehensive set of conduct and organizational rules which can be described as common for financial institutions such as robust governance and internal control arrangements, complaint-handling procedures and conflicts of interest management.
- The white paper for an ART will be subject to increased requirements, mostly to reflect the deviating requirements in relation to the issuer of the ART.

A further sub-category will be **significant ART (SART)**. The EBA will be tasked with classifying ARTs as SARTs based on certain criteria including the size of the customer base, the value of the ARTs issued, the number of transactions, the size of the reserve, the significance of the cross-border activities and the interconnectedness with the financial system.

Issuers of **SARTs** will be subject to the following **additional obligations**:

- The issuer needs to have a remuneration policy that promotes sound and effective risk management;
- The issuer shall ensure that the SART can be held in custody on a fair, reasonable and non-discriminatory basis by crypto-asset custodians, including custodians which do not belong to the same group of companies as the issuer;
- The issuer must implement and maintain a liquidity management policy to ensure redemption requests can be fulfilled; and
- The issuer's own funds requirement is increased.

Specific rules for electronic money tokens (EMT)

In addition to ART, MiCA introduces a specific set of rules for electronic money tokens (EMT).

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EMT may only be offered by **credit institutions** and **electronic money institutions** authorized under the applicable EU laws (and their implementing national law implementations), unless the offer is only made to qualified investors and the average outstanding amount of the EMTs does not exceed EUR 5,000,000.

The rules for EMTs follow the regulatory requirements applicable to e-money under the E-Money Directive (Directive 2009/110/EC), unless MiCA provides for derogations or specifications.

A key element is a mandatory redemption right which must be granted to all holders of EMTs.

Following the approach for ARTs, the EBA may also classify EMTs as significant EMTs (SEMT). The additional rules applying to issuers of SEMTs are similar to those that apply to the issuers of SARTs.

Crypto-asset service providers (CASPs)

A considerable part of MiCA deals with a new regulatory regime for crypto-asset service providers (CASPs). The approach taken by the European legislator mimics the investment services regime of the Markets in Financial Instruments Directive (MiFID) introduced 18 years ago.

Compared to the authorization processes for the issuance of ART, the authorization process for CASPs appears to be less complex and, therefore, provides for shorter processing periods when received by the authorities. Competent authorities shall issue their decision within three months upon submission of a complete application.

CASPs will be registered in the central register maintained by ESMA.

Once authorized, CASPs will be able to provide crypto-asset **services in all EU Member States** based on a **passporting procedure** which allows provisions of services across the EU not later than 15 days following submission of the passport application.

Also similar to MiFID, MiCA provides for general entity-level prudential requirements as well as more specific service-related requirements.

The crypto-asset services covered by MiCA are likely going to be as follows:

- The custody and administration of crypto-assets on behalf of third parties;
- The operation of a trading platform for crypto-assets;
- The exchange of crypto-assets for funds (fiat currency);

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- The exchange of crypto-assets for other crypto-assets;
- The execution of orders for crypto-assets on behalf of third parties;
- Placing of crypto-assets;
- (The transfer of crypto-assets);³
- The reception and transmission of orders for crypto-assets on behalf of third parties;
- Providing advice on crypto-assets;
- (The exchange of crypto-assets for financial instruments);⁴ and
- Providing portfolio management on crypto-assets.

Market abuse prevention

Finally, MiCA will introduce rules on the prevention of market abuse, which most notably include prohibitions of market manipulation and insider trading. Thereby, the markets in crypto-assets are brought to the same level as listed financial instruments.

Timing

It is expected that the provisions regarding asset-referenced tokens and e-money tokens will become applicable 12 months after MiCA comes into force. Other provisions will likely apply 18 or 24 months after MiCA comes into force. If the Regulation is still issued this year, the rules on stable coins will, therefore, apply from late 2023, while the remaining rules will apply not before 2024.

³ Inclusion not yet confirmed.

⁴ Inclusion not yet confirmed.

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