

Regulatory News Alert

ESMA report on crypto-assets

17 January 2019

On 9 January 2019, ESMA and EBA released separately reports on the specific characteristics and use of crypto-assets and the underlying DLTs; the relevance and gaps in existing EU regulations when applied to crypto-assets; as well as divergence in the regulatory approaches adopted by various Member States.

ESMA highlighted that the extent of the gaps in the current regulatory framework regarding crypto-assets depends largely on their legal status and whether they are recognized as a financial instrument.

However, the classification of crypto-assets as a financial instrument is the responsibility of individual National Competent Authorities (NCAs) and their decision depends on the definition of financial instruments adopted when transposing MiFID into national law. While a majority of NCAs would likely view crypto-assets with profits rights attached as a MiFID financial instrument, ESMA found that national approaches vary, causing challenges to both regulation and supervision.

ESMA and EBA believe that the introduction of national bespoke rules for crypto-assets that do not qualify as MiFID financial instruments by some Member States further impedes the creation of a level playing field as well as consistent supervisory approach, across the EU. ESMA therefore believes that the creation of an EU-wide approach is necessary also considering the cross-border nature of crypto-assets.

Under ESMA's views, for **those crypto-assets that qualify as financial instruments under MiFID, a full set of financial rules is likely to apply** to their issuer and/or firms providing investment services or activities in relation to those instruments. These include the Prospectus Directive, the Transparency Directive, MiFID II, the Market Abuse Directive, the Short Selling Regulation, the Central Securities Depositories Regulation, and the Settlement Finality Directive.

ESMA also highlights specific gaps and issues with existing rules, and areas that would necessitate potential interpretation or re-consideration of specific requirements to allow for an effective application of existing regulations. In particular, some of the risks that are specific to their underlying technology may be left unaddressed (e.g. identification of the market operator in the case of "decentralized" business models in the trading platform); or certain existing requirements may not be easily applied or entirely relevant in a DLT framework (e.g. reporting or record-keeping requirements under MiFID II).

Where these assets do not qualify as financial instruments, and do not fall within the scope of other EU rules (e.g. E-money Directive), ESMA believes that the absence of applicable financial rules leaves investors exposed to substantial risks.



For example, **ESMA believes that all crypto-assets and related activities should be subject to Anti-Money Laundering (AML) provisions. ESMA therefore supports the EBA's view that the scope of the AMLD should be reviewed in light of the rise of crypto-to-crypto exchanges** and the FATF's October 2018 recommendations to have the following elements within the scope of AML/Combating the Financing of Terrorism obligations: i) providers of exchange services; and ii) providers of financial services for Initial Coin Offerings.

Finally, ESMA proposes the **introduction of appropriate risk disclosures** as a priority for EU policymakers. Such disclosures should include adequate information in relation to the issuer, the project, the rights attached to the crypto-asset, the underlying technology used and potential conflicts of interest, to ensure that consumers are aware of the risks prior to committing funds to crypto-assets.

How Deloitte can help?

Deloitte can help you to gain awareness on the subject and design with you a pragmatic strategy based on solutions and options to allow you to handle the evolution of this new asset class as well as to identify the potential impacts on the issuance, trading and custody value chain. We will support you on various critical dimensions such as business & operating models, regulatory & compliance, technology, and risk management.

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