



EU Digital Finance Package

Cryptoassets & Markets: an Overview



Agenda

1. Introduction - MEP Ondrej Kovarik (CZ, Renew)
2. About crypto-assets
3. About the crypto-assets market
4. About the crypto-assets use cases
5. Considerations for the policy framework



About crypto-assets

A new assets class with tremendous potential

Crypto-assets

A new asset class with specific characteristics

Very diverse range of assets

What they have in common is that they are **all registered on a blockchain**, which allows, under some conditions:

- **permanence**;
- **direct appropriation**, with no intermediary;
- **uniqueness**; i.e. prohibition of duplication.

Protocol tokens



Synthetic assets



Digital objects (NFTs)



.arianee

DAO tokens



Utility tokens



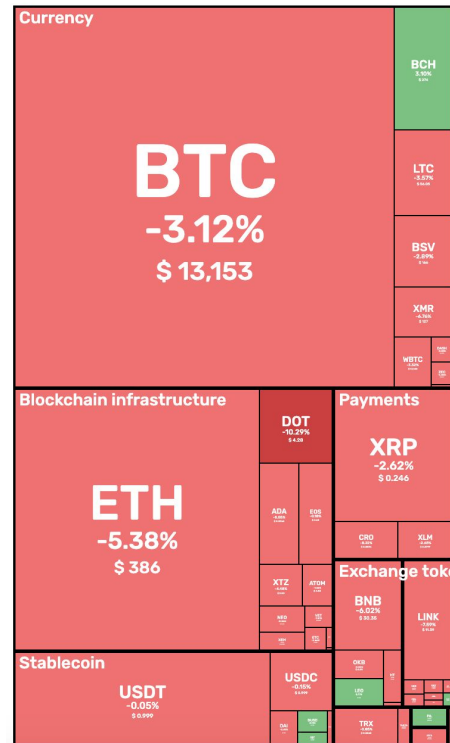
Stablecoin



Securities

Other

Market State Visualization



Crypto-assets

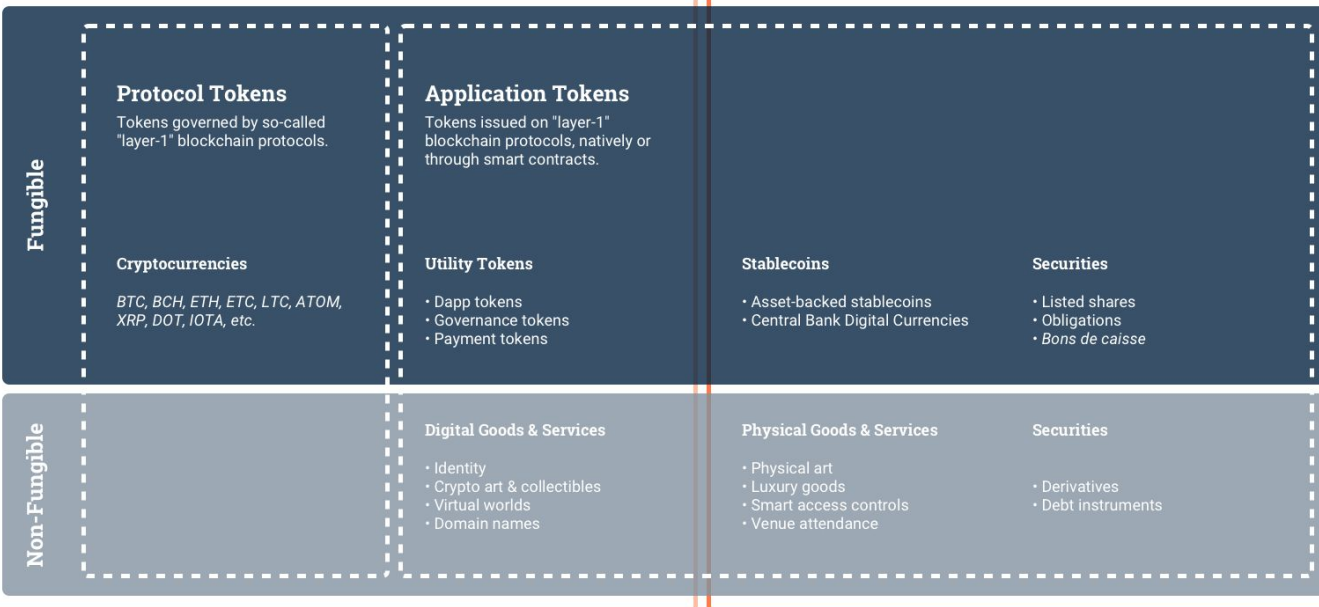
Proposed Taxonomy

Native Crypto-Assets

Assets whose use and value derives entirely from their blockchain representation. They do not require to be linked with an asset or right that exists outside of the blockchain to function.

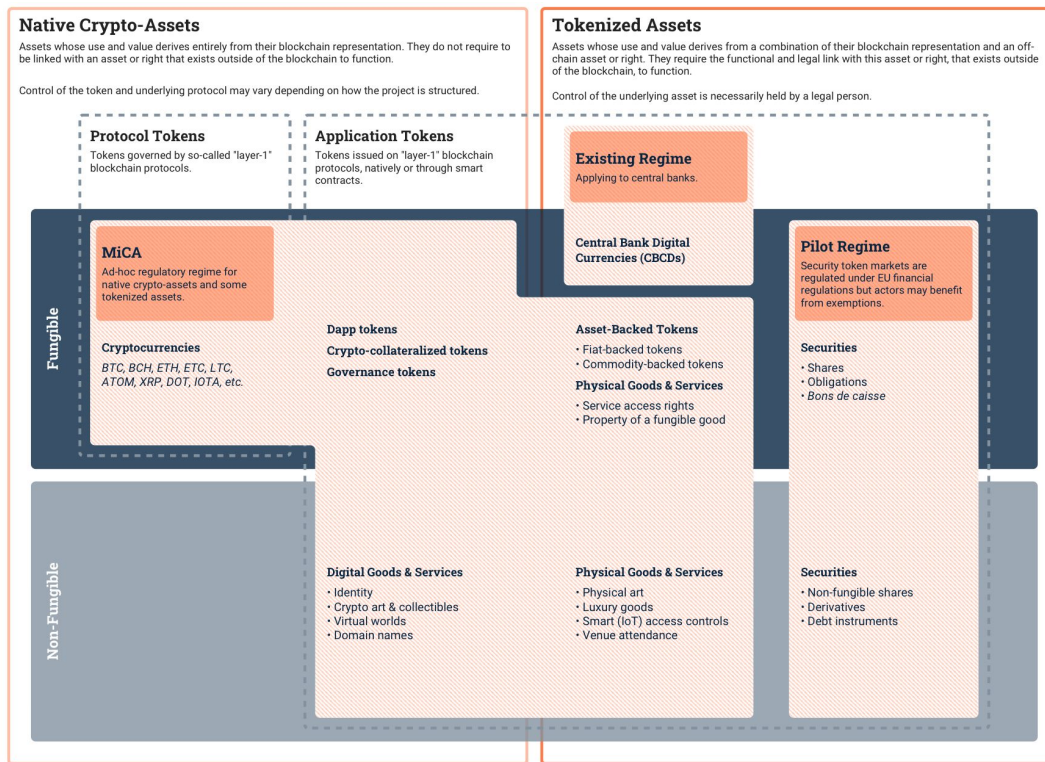
Tokenized Assets

Assets whose use and value derives from a combination of their blockchain representation and an off-chain asset or right. They require the functional and legal link with this asset or right, that exists outside of the blockchain, to function.



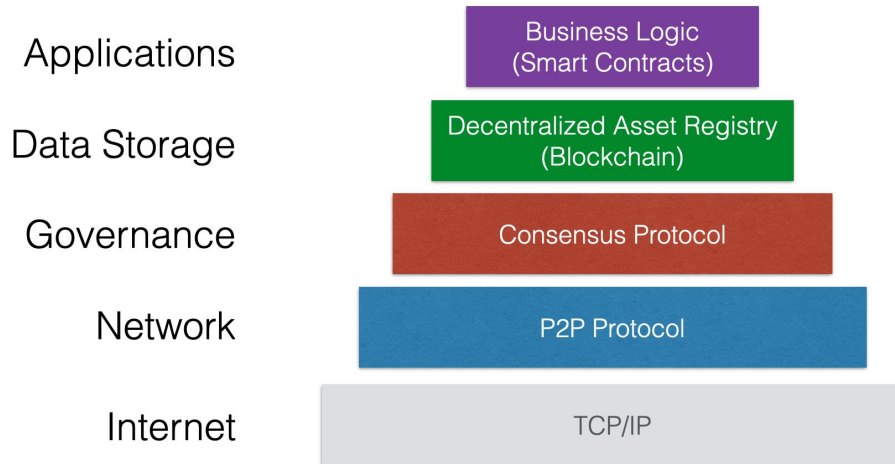
MiCA and Pilot Regime

Illustration of the scope - Assets



Crypto-assets

Key components



- A **virtual Machine** executes the business logic of transactions, referred to as Smart Contracts, the result of which are registered on the blockchain.
- **Blockchain** is the ledger where all the data is stored. This ledger is **distributed** to all the participants.
- **Consensus protocol** ensures that all the participants are behaving in good faith and the blockchain is consistent between all the participants.

Crypto-assets

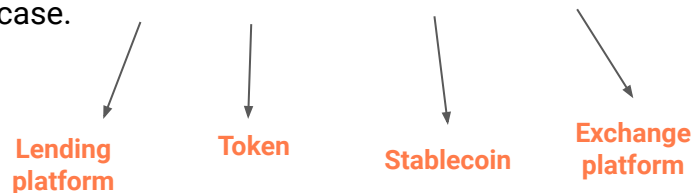
The game-changer: programmability & autonomous execution (“smart-contracts”)

Simple transaction

- Mr. A creates and sends a simple transaction:
Transfer X crypto-assets to Ms. B
- The Virtual Machine executes the transaction.
- The **result** of the transaction is registered on the blockchain.

Smart-contracts

- Actor deploys a complex business logic / program on the blockchain that creates a new use case.



- The protocol adds the smart-contract to the blockchain.
- The smart-contract is part of the blockchain and **any authorized party can use the smart-contract later on. It will be executed by the Virtual Machine.**

=> “Decentralized” use cases



About the crypto-assets market

Booming newcomers, looming incumbents

Crypto-assets

Constant growth and opportunities

7,500+ crypto-assets

**\$400 billion
marketcap**

300+ exchanges



Numbers: October 2020

Source: Coinmarketcap

Crypto-assets

Crypto-assets market vs. traditional markets

S&P 500



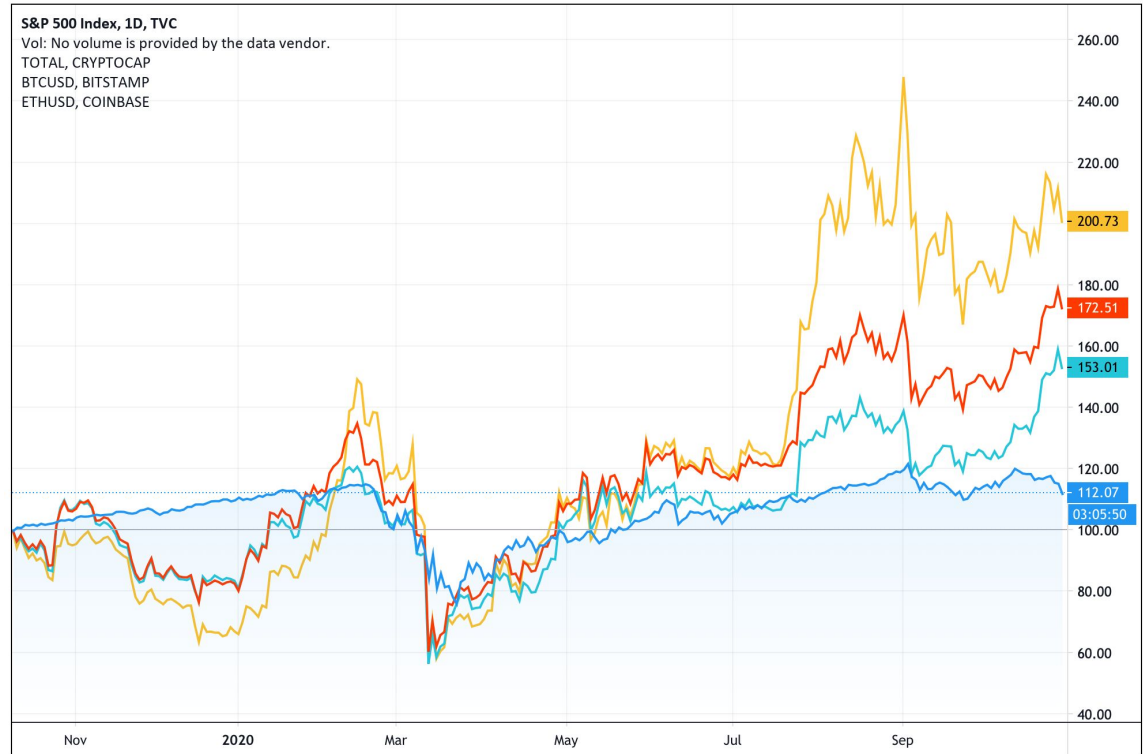
Bitcoin



Ethereum



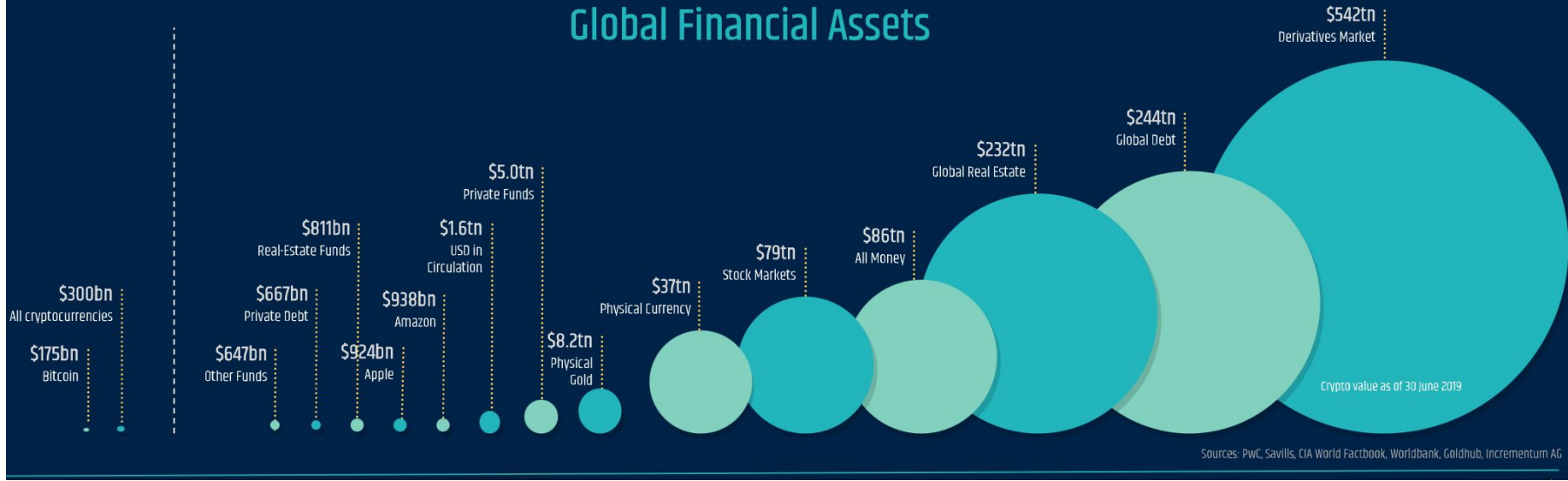
Total Crypto



Crypto-assets

Crypto-assets remain marginal compared to other financial assets in terms of total cap

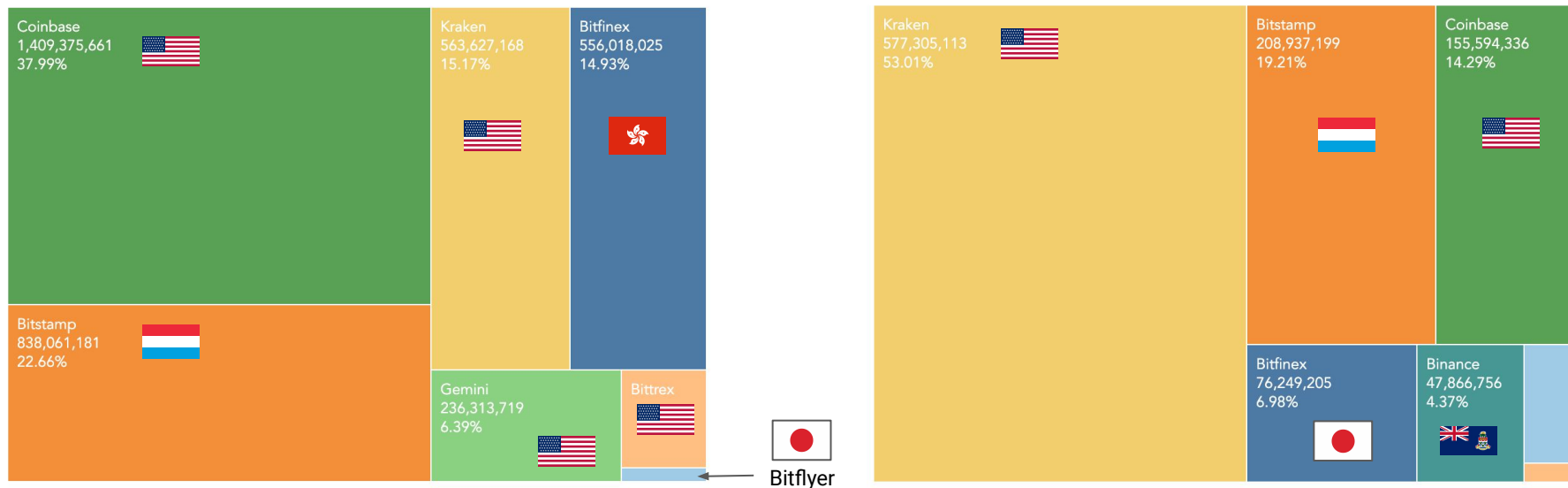
Global Financial Assets



Source: SLIC

Crypto-assets

The biggest crypto-exchanges are located out of the EU



*BTC/USD - Traded volume and market share
(first 2 weeks of October 2020)*

*BTC/EUR - Traded volume and market share
(first 2 weeks of October 2020)*

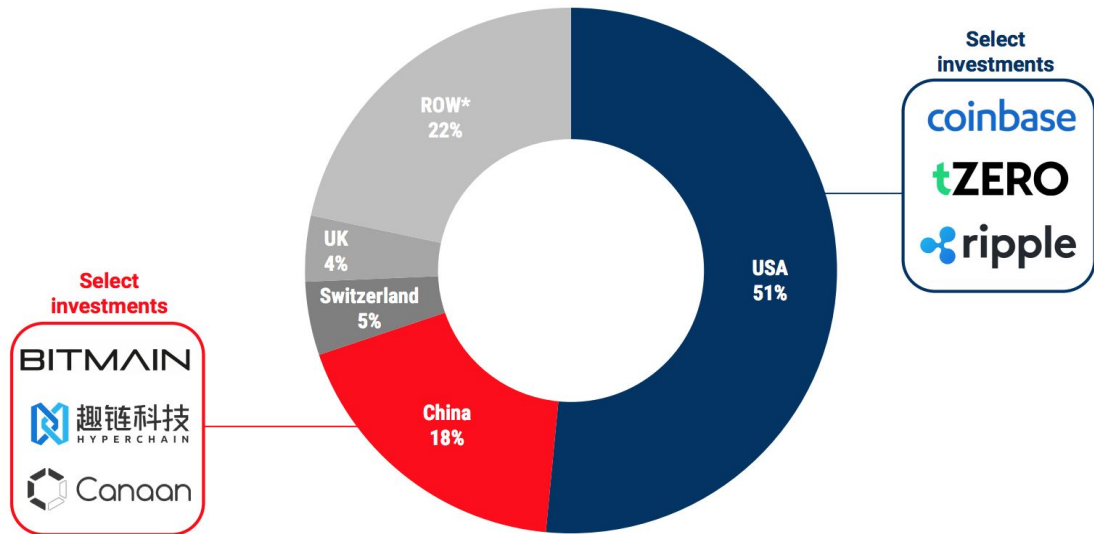
Source: Kaiko

Crypto-assets

The absence of the EU on the funding stage of the crypto industry

Companies in US and China dominate funding

Share of funding dollars by geography, 2015 – 2019



Crypto-assets

Incumbents' growing interest


Published on 23/04/2019

SOCIETE GENERALE ISSUED THE FIRST COVERED BOND AS A SECURITY TOKEN ON A PUBLIC BLOCKCHAIN

Central banks and BIS publish first central bank digital currency (CBDC) report laying out key requirements



Press release | 09 October 2020

 Office of the
Comptroller of the Currency

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PayPal allows Bitcoin and crypto spending

🕒 4 days ago

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News Release 2020-98 | July 22, 2020

Federally Chartered Banks and Thrifts May Provide Custody Services For Crypto Assets

Jack Dorsey says Bitcoin and blockchain will shape Twitter's future where 'content exists forever'

Shalini Nagarajan 29/09/2020, 15:15

 libra

NEWS & ANNOUNCEMENTS

**J.P. Morgan Creates
Digital Coin
for Payments**



About the crypto-assets use cases

Centralized or decentralized?

Crypto-assets

Use cases: centralized or decentralized ?

A significant distinction: centralized ("traditional") and decentralized projects

Centralized

- **Most significant actors**
- Operating **through a dedicated legal entity** which **keeps control on tokens / protocols**
- Activities :
 - Issuer of crypto-assets
 - Custodian
 - Multilateral trading facility
 - Broker
 - Portfolio manager
 - Adviser...

Decentralized

- **Most innovative players**
- **Deploying smart-contracts on the blockchain,** that are ultimately **operated by the final clients who are in control of the protocol / tokens**
- Activities
 - Decentralized Finance (DeFi) - loans, exchanges...
 - Video games
 - Art
 - Coordination mechanisms
 - Insurance...

Crypto-assets

Use cases: centralized or decentralized ?

A significant distinction: centralized ("traditional") and decentralized projects

Centralized

Example:

Bitstamp

- **Exchange platform** / Multilateral trading facility
- **Operated and controlled by a company** (incorporated in Luxembourg)
- **IT:** A centralized database of trades connected to the blockchain for deposits / withdrawals

Decentralized

Example:

 **Uniswap**

- **Exchange** with radically innovative *liquidity pools* (no orderbooks)
- **Operated by smart-contracts** deployed by a company but **not under its control**
- **IT:** Deployed on the blockchain, transactions are sent directly by the user to the smart-contracts.

Crypto-assets

Use cases: what are crypto-assets used for?

Established

Protocols



Market-related services
(primary and secondary
market, custody, portfolio
management, advice)

Bitstamp

Security hardware and
software



Data collection and treatment



Mining / Staking



Emergent

Decentralized Finance



Creation, distribution, sale of
NFTs (unique digital assets)



Collective organizations on
blockchain (DAOs)



Stablecoin issuance



Payment in crypto-assets



Activities related to security
tokens (custody, issuance,
secondary markets, etc.)



Primitives

Digital identity



RegTech



Central Digital Bank
Currencies

Privacy preserving protocols



Decentralized data storage



Decentralized computing
power



Considerations for the policy framework

Crypto-assets regulation as a catalyst for safer innovation

Encourage the benefits while addressing the risks: staying competitive

Benefits

Growth and jobs

Citizen empowerment

Cost reduction

Trust and transparencies

Alternative fundings

Encourage the benefits while addressing the risks: staying competitive

Risks

Security

Infrastructures have been subject to **numerous cyberattacks**

=> addressed with DORA proposal 


Money laundering & terrorism financing

Limited identification / check requirements of participants, lack of clarity behind compliance, supervision of transactions

=> addressed with 5th AML Directive (extension currently discussed) and FATF recommendations 


Investor & consumer protection

Investors/consumers may be exposed to **unprotected, speculative and opaque markets & fundraisings**

= > addressed by MICA 

Financial Stability

The development of this new class of assets and potential alternative means of payments could represent a threat to financial stability

= > addressed by MICA 

MiCA and Pilot Regime

Content of the Draft EU regulation

Two foundational texts to regulate crypto-assets in the EU...

MiCA Regulation ("Markets in crypto-assets")

Regime

Mandatory bespoke regime

Scope - *Crypto-assets*

**Utility tokens, cryptocurrencies
and stablecoins**
(asset-referenced tokens &
e-money tokens)

Scope - *Activities*

Issuance, exchange, custody,
and other "investment services"

Authorised actors

All
except for e-money tokens - restricted to
credit institutions

Pilot regime for DLT market infrastructures

**Transitional regime towards
definitive rules**, granting
exemptions to financial
regulations under conditions

Security tokens (= transferable
securities on blockchain)

Trading on an
MTF

Delivery-
settlement

Investment
firms

Central
Security
Depositories

MiCA and Pilot Regime

Illustration of the scope - Assets

Native Crypto-Assets

Assets whose use and value derives entirely from their blockchain representation. They do not require to be linked with an asset or right that exists outside of the blockchain to function.

Fungible

Protocol Tokens

Tokens governed by so-called "layer-1" blockchain protocols.

Cryptocurrencies

BTC, BCH, ETH, ETC, LTC, ATOM, XRP, DOT, IOTA, etc.

Application Tokens

Tokens issued on "layer-1" blockchain protocols, natively or through smart contracts.

Utility Tokens

- Dapp tokens
- Governance tokens
- Payment tokens

Non-Fungible

Digital Goods & Services

- Identity
- Crypto art & collectibles
- Virtual worlds
- Domain names

Tokenized Assets

Assets whose use and value derives from a combination of their blockchain representation and an off-chain asset or right. They require the functional and legal link with this asset or right, that exists outside of the blockchain, to function.

Stablecoins

- Asset-backed stablecoins
- Central Bank Digital Currencies

Securities

- Listed shares
- Obligations
- *Bons de caisse*

Physical Goods & Services

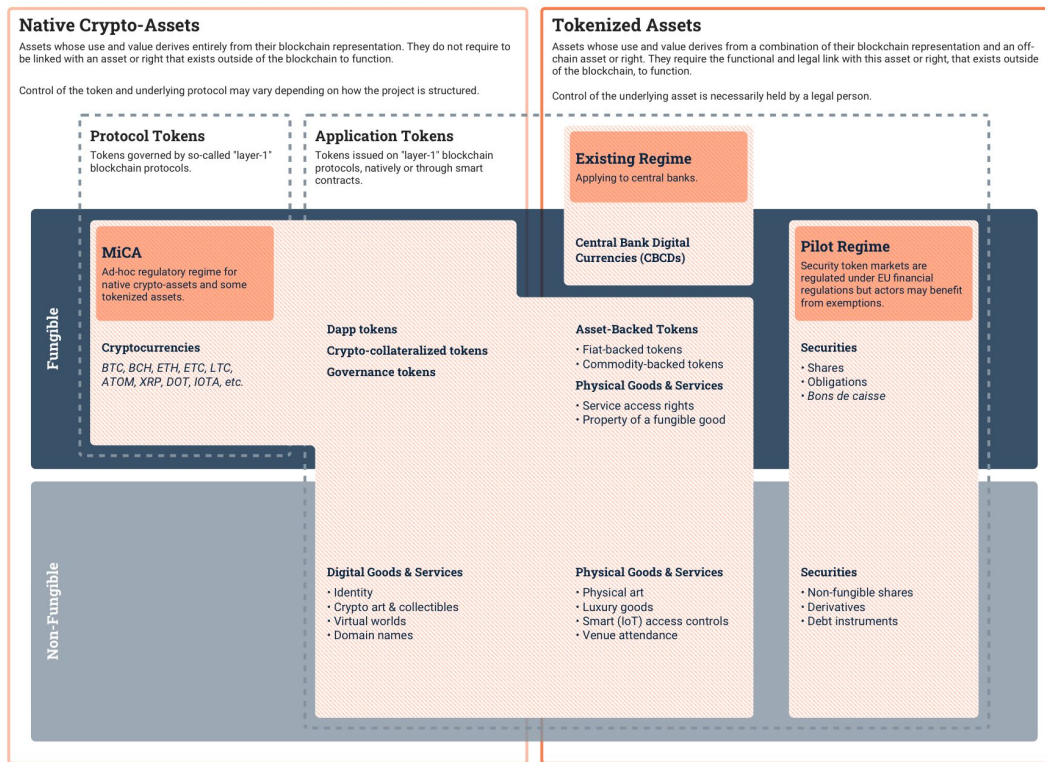
- Physical art
- Luxury goods
- Smart access controls
- Venue attendance

Securities

- Derivatives
- Debt instruments

MiCA and Pilot Regime

Illustration of the scope - Assets



MiCA and Pilot Regime

Illustration of the scope - Activities

The current scope

Centralized

Bitstamp

- Covered by the regulation
- Can comply with no major issue
- Article 68: ban from listing assets that have been issued with no whitepaper

Decentralized

 Uniswap

- **Not excluded** => in the scope?
- Can not respect obligations that imply a **control** over the assets listed, the operations, etc.
- **Illegal in the EU?**

MiCA and pilot regime

What's missing - entirely or in part - for a perfect EU regime?

Equal opportunities between incumbents and newcomers

Barriers to entry high for newcomers, and low for incumbents.

Proportionality

The proportionality is insufficient to cater for different business models in the sector

Allowance for DeFi and other decentralized use cases

Innovation takes place through increasingly decentralised use cases (e.g. so-called decentralised finance, or "DeFi"). Current drafting does hinder or ban those use cases - probably as an unwanted side effect.

Adapted operational requirements

Certain operational requirements are very costly and out of sync with market practice.

Authorization of public blockchains

Public blockchains are not recognized as platform for most innovative use cases.

THANK YOU



Simon Polrot,
President, ADAN

simon.polrot@adan.eu



Florian Glatz, President,
German Blockchain
Association

florian@bundesblock.de



Amandine Doat,
President of EU Affairs
Committee, ADAN

amandine.doat@adan.eu



Marina Markežič, Board
member, Blockchain
Think Thank Slovenia

[marina.markezic@
blockchainthinkthank.si](mailto:marina.markezic@blockchainthinkthank.si)