Latest Policy Developments for DLT

International Association for
Trusted Blockchain Applications

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Prepared exclusively for INATBA Members.

Content

Highlights: INATBA Policy Developments

INATBA continues to work on its Policy Position and response to eIDAS. The Identity Working Group is also developing an outreach and advocacy strategy for eIDAS. Members who would like to get involved in the work or get more information should contact the co-chairs of the Identity Working Group.

The Finance Working Group is working on their DeFi-related outputs, including a focus on DeFi and DAOs, NFTs and a regulatory proposal. Members are also working on the AMLR initial output and follow-up, plus a comparison between INATBA policy proposals on the PRR and the final PRR output. Contact xenofon.kontouris@inatba.org to get involved.

Highlights: EU and US Policy Developments

This is INATBA's bi-weekly newsletter covering policy developments which affect Distributed Ledger Technology (DLT) and its applications in the EU And US. It covers the period from the 07th January until 21st January 2022.

Brussels has definitely come back at full speed, with the ECON Committee of the

European Parliament approving the text of trilogues on the DLT Pilot Regime and near-finalising amendments on the future Crypto-Assets Regulation, while the ECB hurled some hard language on Bitcoin. On the week of 24th , the trilogues on DORA will begin. This means that for all MiCA, DORA, and the EU Travel Rule, we have a more tangible schedule of these rules becoming applicable.

Over in the US, the year started with a bang as several Members of Congress introduced legislation on digital assets. Congress is also set to hold hearings on various crypto issues in the next few months. House Financial Services Committee Chairwoman Maxine Waters (D-CA) has said she plans to focus on crypto this year and will likely introduce legislation based on the President's Working Group (PWG) stablecoins report recommendations.

Regulators also continue to express an interest in crypto, as the Securities and Exchange Commission (SEC) and Office of the Comptroller of the Currency (OCC) continue to discuss the industry. The Federal Reserve (the Fed) released its highly anticipated study of a central bank digital currency (CBDC). The study did not make a final recommendation but laid out the pros and cons of CBDC and asked for public comment.

EU Policy Developments

MiCA: Update on amendments

On the week of 17 January, a non-public document of the latest amendments on the Markets in Crypto-assets (MiCA) regulation proposed by Members of European Parliament (MEPs) was circulated. According to the latest amendments INATBA's policy positions have been addressed as follows:

- On **activity-based definitions**, the European Parliament has proposed that a crypto asset is token used for "direct investment or finance purposes", while an e-money token (EMT) is mainly "used for payment", making all non-payment stablecoins potentially asset referenced tokens (ARTs).
- On the **legal entity requirements for Decentralized Autonomous Organisations** (DAOs) a clarification has been added for decentralized issuers of crypto-assets to not be required to organise in a single legal entity and to not be subject to regulation until the offering of the crypto-assets to the public is centralised. Additional clarification has been added for crypto-assets managed by DAOs, provided that such crypto assets are compatible with the requirements of MiCA and do not pose a risk for financial stability, market integrity or investor protection, can be admitted to trading on a European trading platform for crypto-assets.
- On **exemptions for credit institutions**, the Parliament proposes that credit institutions authorised under the Capital Requirements Directive (CRD) should not need another authorisation under MiCA to issue ARTs. They should, however, notify at least three months prior to the issuance their respective competent authority of their intention to issue an ART.
- Finally, on **capital raising thresholds** amendments have been introduced to increase the capital raise for projects using DLT/blockchain technologies to a ceiling of EUR 5M within 12 months without a full prospectus (up from EUR 1 M).

DLT Pilot Regime: Trilogue Agreement

The Economic and Monetary Affairs Committee (ECON) voted on the provisional agreement resulting from trilogues on the Proposal for a Pilot Regime for Markets Infrastructures based on Distributed Ledger Technology (also known as the DLT Pilot Regime). As expected, the ECON Committee approved with a simple majority (47 votes in favour, 3 votes against and 7 abstentions) the agreement reached with the co-legislators. The provisional agreement will have to be voted now in the Plenary Session of the European Parliament, a process that unless there are surprises, should be a mere formality. This will most likely take place during February's Plenary Session.

Crypto Assets: ECB Comments

In a column series, prominent members of the European Central Bank (ECB) in charge of the current development of the Digital Euro published their considerations on the Bitcoin and the it future utility for society and investments. The column states that the Bitcoin has signalled the potential benefits of DLT but it has failed to deliver on its promises, coming at high cost to retail investors, while also facilitating illicit activities. Importantly, it is noted that Bitcoin has a high social cost, with thenegative net social value not being perceived by Bitcoin investors who believe them to be covered by current and future speculative gains, without these gains being realised. Consumer protection is also at the forefront, as the authors percieve Bitcoin to be a risk for retail investors as they stand to lose “their hard-earned savings for the benefits of smarter Bitcoin investors who bought at low and sold at high prices”. In addition, they also note that it has environmental negative externalities due its high energy consumption due to the proof of work mechanism. While the columns carry the usual disclaimer that views expressed are “not necessarily the ones of the ECB,” the authors are all key contributors to the ECB’s work on the digital euro.

Crypto Assets: Russian Central Bank comments

On 20th January, the Russian Central Bank published a consultation paper in which it proposes a ban on the use and mining activities of cryptocurrencies on Russian territory, under the arguments that these assets pose threats to financial stability, citizens’ wellbeing and the overall monetary policy sovereignity. The consultation paper proposed to ban financial institutions from carrying out any operations with cryptocurrencies and additionally develops the possibility of banning financial actors from buying or selling cryptocurrencies for fiat curencies.

Crypto Assets : IMF comments on crypto and investment portfolio

On 11th January, the International Monetary Fund (IMF) published a blog on the possibilities of crypto on investment portfolios. the IMF underlines that the value of Bitcoin and other cryptocurrencies are moving more in lockstep with market swings in the stock market and therefore serve as a poor hedge for investment portfolios. The blog entry argues that the correlation of crypto assets with traditional holdings like stocks has increased significantly, which limits their perceived risk diversification benefits and raises the risk of contagion across financial markets. It also highlights that this trend is “also apparent in emerging market economies,” where the take-up of cryptocurrencies is much stronger.

DORA: Trilogues to begin

The kick-off meeting for the negotiations between the three EU legislators, the Commission, the Parliament and the Council, on the Digital Operational Resilience Act (DORA) will take place on 25th January. The non-public agenda includes most of the relevant and contentious points as raised and seen in the different versions of the regulation by the co-legislators. This meeting will focus on the scope and proportonality, the ICT risk management framework, digital resilience testing, contractual arrangements with third-party service providers, the oversight framework and the DORA and Network and Information System alignment. On hte other hand, the technical trilogue will include the interaction between the Central Securities Depositories Regulation (CSDR) and DORA. These negotiations are expected to last until well into the second quarter of the year. The French Presidency has been very vocal on their goal to finish the negotiations on the file under its Presidency. Also, the negotiations will focus on the implementation date of the regulation, with the Council and the Parliament pushing for an implementation date of 24 months after the publication in the Official Journal of the EU, on this point, the Commission originally proposed an implementation date of 12 months.

AML: European Parliament Timelines

We have seen non-public document providing an overview of the timetable for the procedure on the proposal for the establishment of the new Authority for Anti-Money Laundering (AMLA), Anti-Money Laundering Regulation (AMLR) and the recast of the Transfer of Funds Regulation (TFOFR) in the European Parliament (EP). All three proposals are subject to a joint committee legislative procedure where the EP's position on the Commission's proposals is being developed jointly by the Economic and Monetary Affairs Committee (ECON) and the Committee on Civil Liberties, Justice and Home Affairs (LIBE). Rapporteurs on the AMLA proposal, Luis Garicano (Renew, ECON) and Emil Radev (EPP, LIBE), will have the first shadow meeting on 25 January 2022. The draft report is expected for mid-march and the consideration of amendments is scheduled for May. The Final Report, including compromise amendments will be voted in ECON-LIBE committee by the end of June and discussed during the Plenary Session of July.

On the AMLR, Rapporteurs Eero Heinaluoma (S&D, ECON) and Damien Careme (Greens, LIBE), held the first meeting with Shadow Rapporteurs on 12 January in which they discussed the timetable and the main priorities of the draft regulation. The Draft Report is expected for the 18th of February/2nd of March. The Final Report, including compromise amendments, and vote in ECON-LIBE is expected for late June/early July. The Plenary vote is being indicatively scheduled during the July or September Plenary.

On the TFOFR, Rapporteurs Ernest Urtasun (Greens, ECON) and Assita Kanko (ECR, LIBE) are in the process of holding meetings with Shadow Rapporteurs and stakeholders until the end of January. The Draft Report is expected for the 7th of February. The Final Report, including compromise amendments, and vote in ECON/LIBE is expected for the 31st of March. The Plenary vote is being planned for early April.

Looking Ahead

25 January 2022	• ECON Committee meeting: Economic dialogue with Bruno Le Maire, ECOFIN President.
26 January 2022	• Coreper II
27 January 2022	• Working Party on Financial Counsellors
28 January 2022	• Coreper II
02 February 2022	• Coreper II
02 February 2022	• Financial Services Committee
04 February 2022	• Coreper II

US Policy Developments

Congress

As we kick off 2022, several members have introduced and announced intentions to introduce legislation pertaining to crypto, such as on central bank digital currency (CBDC) and stablecoins. So far, all the introduced and upcoming bills are partisan and lack co-sponsors, making the likelihood of real traction dim. The bills also face an uphill battle as Congressional members are likely to start focusing on the midterm elections in June, and Congress has other more crucial priorities such as flood insurance reauthorization.

Rep. Tom Emmer (R-MN), co-chair of the Blockchain Association and vocal crypto advocate, introduced a bill prohibiting the Federal Reserve from issuing a CBDC directly to individual consumers. The bill points out concerns over privacy and cybersecurity why the Fed should not issue a CBDC. The bill also argues that the Fed issuing a CBDC would put the Fed "on an insidious path akin to China's digital authoritarianism." The bill would recommend that any CBDC issued from the Fed must be open, permissionless, and private. The bill was introduced on January 12.

Rep. Josh Gottheimer (D-NJ) is reported to be introducing a bill requiring a stablecoin issuers to either become a bank or partner with a bank, a recommendation put forth in the President's Working Group (PWG) report on stablecoins. The bill would require stablecoin issuers to operate as a traditional bank with deposit insurance. The bill could be released in its official text in the coming weeks. The bill is likely to gain traction within the Democratic party unless House Financial Services Committee Chairwoman Maxine Waters (D-CA) introduces a competing, more comprehensive bill that acts on the same recommendations from the PWG report.

Top Democrat and Republican leaders of the House and Senate Agriculture committees on January 12 wrote a joint letter to newly sworn-in Commodity Futures Trading Commission (CFTC) Chair Rostin Behnam about digital assets. Senate Agriculture Chair Debbie Stabenow (D-MI), House Agriculture Chair David Scott (D-GA), Ranking Members John Boozman (R-AR), and Glenn "GT" Thompson (R-PA) asked what powers Behnam needs to regulate the digital assets industry properly. The letter also asked how the CFTC works with other agencies to on fraud and cybercrime in decentralized finance (DeFi). The letter called for the CFTC to relay the benefits and the risks of digital assets to the committee.

The letter comes as the Senate Agriculture committees and the CFTC Chair Behnam have called for more industry jurisdiction. The letter comes as policymakers across several committees and regulators are engaged in a turf war for oversight of crypto.

The House Energy and Commerce Subcommittee on Oversight and Investigations convened a hearing titled "Cleaning Up Cryptocurrency: The Energy Impacts of Blockchains" to discuss the energy consumption of Bitcoin mining. In the staff memo, lawmakers appeared clear: lawmakers are concerned about bitcoin mining emissions and, in turn, the mining facilities used to power these networks. During the hearing several members showed a deep understanding of the topic, asking about the motivation of miners to use fossil fuels, the technical process of bitcoin mining, and the energy consumption of bitcoin mining before China banned the industry. The hearing was largely a fact-finding hearing and ended with no mention of specific legislation or concrete next steps.

Securities and Exchange Commission (SEC)

A federal judge overseeing a court battle between the Securities and Exchange Commission (SEC) and blockchain company Ripple has ordered the agency to turn over internal documents to shed light on how officials developed their views on digital assets. The verdict of the court battle is highly watched as its results could have far-reaching implications for the regulation of crypto currencies. The judge also ordered the SEC to produce an email containing a draft of a speech by former Division of Corporation Finance Director William Hinman. With federal crypto regulation mainly being influenced by regulation through enforcement, the result of the court cases will include a decision on whether Ripple's XRP is a security, which could distinguish clarification over the turf war between the Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC).

During a recent interview, SEC Chair Gary Gensler declined to say whether Ethereum is a security and covered by the agency's strict trading rules. Gensler claimed he does get involved in public forums, despite previous public comments on the industry.

Democratic SEC Commissioner Allison Lee said that her agency doesn't need to update its rulebook to oversee digital assets. Lee's statement further highlights the SEC's desire under Gensler not to create any new, significant laws specific to crypto despite other bodies calling for new regulations for the asset class.

On January 19, Gensler spoke at the Exchequer Club, a financial industry group. While his opening statements mainly consisted of previous comments, the Q&A section was primarily focused on crypto. The questions included pushback on ambiguity, enforcement, and engagement. He maintained that regulators like himself are left to fill in the blank when Congressional actions leave ambiguity in laws and stressed that there were rules in place. He added that crypto companies often use public funding such as initial coin offerings (ICOs) but do not file with the agency. He argued that crypto is rarely used as a payment method but is used as "digital gold" and is an investment contract under the Howey Test. Gensler also stated that the agency is looking at drafting regulations targeting cryptocurrency but did not provide specificities. Gensler called stablecoins highly speculative stores of value and used quotes when calling them stable. He noted that stablecoins bring up three important areas of questions: 1) money creation; 2) Illicit financing (stated many digital wallets operate outside of the AML regime); and 3) investor protections. He stressed most stablecoins are already securities since most of the stablecoins operate within exchanges.

Commodity Futures Trading Commission (CFTC)

In a speech to the Chamber of Digital Commerce, Commodity Futures Trading Commission (CFTC) Commissioner Dawn Stump said that the CFTC "must urgently consider fine-tuning its rulebook." She said that the CFTC's reliance on enforcement actions to regulate the industry was harmful and not sustainable. Stump's comments come as CFTC Chair Rostin Behnam urges Congress to give his agency greater authority to oversee the crypto industry.

Federal Reserve (Fed)

Federal Reserve Chair Jerome "Jay" Powell's nomination hearing to be Fed Chair for another term touched several crypto-related issues. After Sen. Mike Crapo (R-ID) brought up the topic of a Fed central bank digital currency (CBDC), Powell promised that the industry can expect the Fed -MIT report on a CBDC in the coming weeks. Powell first announced the report would come out in the summer of 2021 and then the fall. Still, he appeared more confident during the nomination hearing. After Senate Banking Chair Pat Toomey (R-PA) asked if a Fed CBDC could exist alongside private stablecoins, Powell assured Toomey they two are not mutually exclusive.

During an exchange with Sen. Cynthia Lummis (R-WY), Powell indicated he might give Wyoming crypto banks access to the Federal Reserve's master account rails in the exchange. Powell also noted that the Fed is making progress on this issue. Sen. Lummis has been vocal that she will hesitate to support Powell's renomination if he does not support granting accounts to crypto banks in Wyoming and will continue to press him on the issue.

The Fed released its long-awaited study of a digital dollar to solicit public comment. The goal of this study is not necessarily intended to have policy outcomes, and the Fed states that it will not proceed without a clear mandate from Congress, preferably in the form of a specific authorizing law. The report looks at the current payment system and outlines the benefits and downsides of a Central Bank Digital Currency (CBDC). At the end of the report, the Fed solicits public comment on 22 questions and requests answers by May 20, 2022, and states that it will be convening public forums to foster further discussion on CBDC.

The Fed did not decide whether it will pursue a CBDC, nor has it decided on a CBDC design option, but it did lay out four key characteristics that a CBDC must adhere to. A CBDC would not require mechanisms such as deposit insurance to maintain public confidence, nor would a CBDC depend on backing by an underlying asset pool to maintain its value. The CBDC would be a liability of the Federal Reserve and would be considered the safest digital asset available to the public, with no associated credit or liquidity risk. The Fed clarifies its preference of a CBDC over private digital money, such as stablecoins and other cryptocurrencies.

If confirmed, Biden's Fed vice chair for supervision nominee Sarah Bloom Raskin would play a central role in writing and shaping the new U.S. regulation for the crypto industry. Her nomination path will likely be contentious, and her views are largely unknown on the topic.

Office of the Comptroller of the Currency (OCC)

FTI Consulting and the British American Business held a panel last week on "The Future of Crypto-Assets and Regulation," where Acting Comptroller Michael Hsu was the keynote speaker. Hsu reiterated that the underbanked and minorities have been especially interested in crypto while pointing out that the industry has encountered a series of scams, hacks, and other disruptive events. He highlighted a good reason stablecoins are receiving the most attention from regulators, calling stablecoins the "oxygen of the crypto ecosystem and serve as a key link to the fiat currency world." Hsu also discussed the risks stablecoins pose, such as the fear that the trust associated with stablecoins could eventually trigger a run like the 2008 financial crisis (a comparison he has made on several occasions). He emphasized the way to prevent a run is through bank regulation, stating that bank regulation would "give credibility to the "stable" part of stablecoins." Hsu once again called for agency coordination to handle crypto. He ended his opening remarks reiterating that the innovation in crypto is exciting and presents a host of opportunities to banks.

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