Latest Policy Developments for DLT

International Association for
Trusted Blockchain Applications

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Prepared exclusively for INATBA Members.

Content

INATBA Policy Developments

The Identity Working Group of INATBA continues its advocacy outreach for eIDAS, the European Commission's proposal on establishing a framework for a European Digital Identity. Previously, the Identity Working Group worked on the Policy Positions and response to eIDAS. Please contact the co-chairs of the Identity Working Group for more information.

The Finance Working Group's focus remains on the AMLR and the DeFi output. The SubWG2 is still working on the initial and the in-depth outputs. SubWG1 is concentrated on DAC8 (taxation of crypto-assets) exclusively. The group aims to provide as much valuable feedback to the policymakers before they finish and publish the document.
To get involved, please contact xenofon.kontouris@inatba.org.

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 4th February until 18th February 2022.

In Brussels the new draft report on the Transfer of Funds Regulation by the European Parliament has been published, with some aspects diverging from the previously seen version of the Council. Also, the European Commission has signaled its intention to develop legislation regarding the possible implementation of the Digital Euro. Also, some Member States developed a non-position paper on the scope of the Anti-Money Laundering Authority.

In the U.S., Congress continues to focus its attention on stablecoins this year, with two hearings on the President's Working Group (PWG) taking place before the House Financial Services Committee and Senate Banking Committee. Additionally, Rep. Josh Gottheimer (D-NJ) released the first bill addressing the PWG report, which outlines the need for a new regulatory structure for stablecoins. The industry is still awaiting the White House's executive order on digital assets.

EU Policy Developments

Digital Euro: European Commission to propose legislation

The Commission announced during a conference, that it will be proposing a European legislation for the Digital Euro. The legislation is expected in the first 3 months of 2023. Currently, the European Central Bank (ECB) is already in its investigative phase which will run until 2023, with a final decision expected by 2025. In this context, the purpose of the Commission's legislation will be to lay down the legal foundations and address any regulatory concerns/issues that would be needed to deploy the digital euro. This piece of legislation will need to go through both decision-making bodies, Council and European Parliament, and it make take some time due to procedure with the final timing potentially matching the timeline set by the ECB.

AMLA: Non-paper from Member States criteria for direct supervision.

A non-public non- paper from Austria, Germany, Italy, Luxembourg, Netherlands and Spain on the scope of the Anti-Money Laundering Authority's (AMLA) direct supervisory powers was circulated. The non-paper contains suggestions to amend the proposed framework for the direct supervision of entities in the Commission's AMLA proposal, by incorporating additional risk-based criteria when defining which entity is to be directly supervised by AMLA. They also call for direct supervision to be exercised based on risk-based criteria rather than focussing on quantitative criteria (size and geographic implantation). Additionally, the non-paper calls for AMLA to directly supervise the assessed cross-border groups or obliged entities presenting the highest risk profile. Finally, the non-paper touches upon the notion of group, indicating that it should also include EU undertakings with parent undertakings or head office entities that are not a credit or financial institution.

TFOFR: European Parliament's Draft Report

On 7 February, the European Parliament published its draft report on the Transfer of Funds Regulation (TFOFR). Compared with the version seen from the Council and the Commission, the following are of note:

- Like Council, Parliament has also removed the threshold of EUR 1000 on concerns that, compared to wired transfers, crypto transfers can more easily obfuscate the ultimately originator or beneficiary of a transfer.

- EP calls on originating CASPs to not make available the accompanying information and/or the crypto-asset transfer itself to the beneficiary if there are doubts to the compliance, including with GDPR, of the receiving CASP.
- A new Article 18 requests the European Banking Authority (EBA) to set up a register of non-compliant Crypto Asset Service Providers (CASPs);
- While EP calls for the provision of the unique transaction identifier in the case the transfer is made from an unhosted wallet, it goes to limit liability of the CASP participating in the transaction.
- Finally, the Parliament calls on the review clause for the Commission to publish a report with several new assessments and analysis two years after the entry into force of the Regulation.

Digital Sovereignty: EBA's launch of its central database

The French Council Presidency held a conference titled as 'Building Europe's Digital Sovereignty', where representatives from the industry shared impressions with policymakers and representatives of European agencies. Among the different topics covered, the Member of European Parliament Miapetra Kumpula-Natri (S&D, NL) advocated for a trustworthy data space in Europe, where owning the infrastructure means owning European sovereignty, and being able to choose providers. This sentiment was supported by Francesco Bonfiglio, GAIA-X CEO, who called for a development of a framework of governance for distributed data. Regarding the security aspect of data, Juhan Lepassar, Director General of ENISA, announced that a cybersecurity certification scheme is being developed for cloud service providers.

Crypto rules: European Commission's comments on transparency

On 7 February, Mairead McGuinness, Commissioner for Financial Stability, Financial Services and Capital Markets Union responded to a question submitted by Eva Kaili (S&D, HE) a Member of the European Parliament on the EU transparency rules for crypto assets. McGuinness said that the Commission has opted for the "necessary" level of protection and information for retail consumers, and the EU crypto rules requiring providers to publish pricing policies allow professional and retail clients of CASPs to be informed upfront and to decide easily on the provider.

Crypto assets: Warning by the Financial Stability Board

On 16 February, the Financial Stability Board (FSB) published a report mentioning that fast-moving crypto assets could threaten the financial system as they expand into the conventional financial system. The report examines governance, risk management, and operational resilience in assets such as Bitcoin, less volatile stablecoins, and decentralized finance that uses distributed ledger technology. It notes the close, complex, and constantly evolving interrelationship between these three segments, which need to be considered holistically when assessing related financial stability risks. These risks could escalate rapidly, and the FSB calls for a timely and pre-emptive evaluation of possible policy responses, with the caveat that the rapid evolution and international nature of crypto-asset markets raise the potential for regulatory gaps.

Looking Ahead

21 February 2022	• Coreper II
22 February 2022	• Working Party on Financial Counsellors
22 February 2022	• Financial Services Committee
23 February 2022	• Coreper II
25 February 2022	• Coreper II
25 February 2022	• Informal meeting of Ministers of Economy and Finance
02 March 2022	• Coreper II
22 February 2022	• Working Party on Financial Counsellors
22 February 2022	• Financial Services Committee
23 February 2022	• Coreper II

US Policy Developments

White House

The anticipated White House executive order on digital assets will cover a range of digital asset and digital asset-related topics. The report is expected to include a commission of a central bank digital currency (CBDC) study- separate from the Federal Reserve- and ask agencies- including the Departments of Justice and Homeland Security- to develop reports on the future of digital assets. In parallel, the Director of the Office of Science and Technology Policy will conduct a technical assessment of what is required to support a CBDC system, similar to the Boston-Fed MIT study.

Additionally, the Attorney General, along with the Federal Trade Commission (FTC) and Consumer Financial Protection Bureau (CFPB), will be asked to examine the impact of the growth in digital assets on market competition. The Securities and Exchange Commission (SEC), Commodity Futures Trading Commission (CFTC), Federal Reserve, Federal Deposit Insurance Corporation (FDIC), and Office of the Comptroller of the Currency (OCC) are expected to weigh in on market protection measures within their jurisdictions. Treasury, the SEC, the CFTC and federal banking agencies, will work on reports on how to protect against risks involved with cryptocurrencies. The Federal Trade Commission (FTC) and CFPB will be asked to look at privacy issues related to cryptocurrencies.

Finally, the report will address U.S. global competitiveness within the digital assets industry by examining a coordinated global approach for standardizing crypto rules. The State Department, Treasury, Commerce Department, and United States Agency for International Development (USAID) will work to create a framework for interagency international engagement with foreign counterparts in an international forum to enhance the adoption of digital assets and standardize rules.

The release date of the executive order is still unknown. Bloomberg reported of a disagreement between the White House and Treasury Secretary Janet Yellen over the scope and discussions on a CBDC. According to the Bloomberg article, Yellen believes that the Federal Reserve, which released a report on the topic last month without making a conclusion on the topic, should be given more time to develop its thinking on the topic. The White House wants to make a more concrete conclusion about a potential CBDC.. Additionally, Treasury has stated that regulators are already working on providing the industry with more clarity about digital assets, making a report unnecessary. Although there are anonymous reports of private bickering over the Biden administration's approach to digital assets, official White House and

Treasury spokespeople deny these reports and said the administration is united in its work on digital assets.

White House

The first piece of legislation addressing the recommendations in the President's Working Group (PWG) report on stablecoins was introduced February 15, 2022, by Rep. Josh Gottheimer (D-NJ). The released draft text would set up a new regulatory structure for certain stablecoins, including government-backed insurance akin to such insurance for bank deposits. Gottheimer expects a House Financial Services Committee markup on stablecoin legislation and broader crypto policy in the next couple months.

Rep. Warren Davidson (R-OH), a crypto advocate, introduced the "Keep Your Coins Act", prohibiting regulators from limiting users' use of convertible virtual currencies to buy goods or services. Additionally, the bill prevents agencies from restricting transactions through a self-hosted or "unhosted" wallets. The bill was introduced in response to concerns by Rep. Davidson regarding Treasury Secretary Janet Yellen's restricting cryptocurrency, and recent discussions about the Financial Crimes Enforcement Network (FinCEN) reexamining a controversial rule requiring a know-your-customer requirements (KYC) for un-hosted or self-hosted crypto wallets.

Senators Jim Risch (R-ID), Bob Menendez (D-NJ), and Bill Cassidy (R-LA) introduced the "Accountability for Cryptocurrency in El Salvador (ACES) Act", which would require a State Department report on mitigating risks to the U.S. financial system from El Salvador's adoption of bitcoin as legal tender. The Senators stated El Salvador's recognition of bitcoin (BTC) as official currency invites money laundering and undermines U.S. interests. The proposal received quick backlash from El Salvador President Nayib Bukele, who said the Senators' have zero jurisdiction on a sovereign and independent nation.

On February 8, 2022, the House Financial Services Committee convened a hearing entitled "Digital Assets and the Future of Finance: The President's Working Group on Financial Markets' Report on Stablecoins." The only witness was Nellie Liang, Under Secretary for Domestic Finance at the Department of the Treasury. There was not a consensus among committee members that stablecoin issuers do needbank-like regulation , but most agreed that stablecoin issuers should conduct audits and make disclosures. For example, Rep. Gregory Meeks (D-NY) argued that limiting stablecoin issuance to insured depository institutions (IDIs) would raise barriers to the financial system, especially for marginalized groups. It was evident that members were more engaged, educated, and interested in stablecoins during this hearing than prior hearing. Rep. Joyce Beatty (D-OH) said she previously thought of stablecoins as the "Wild West" but now sees them as the future frontier. Despite discussions on introducing legislation, there is still no clear sign that there will be stablecoin legislation introduced anytime soon.

On February 9, 2021, the Senate Agriculture Committee conducted a hearing entitled "Examining Digital Assets: Risks, Regulation, and Innovation". The hearing was attended by witnesses from the public and private sectors, including Commodity Futures Trading Commission (CFTC) Chairman Rostin Behnam and Sam Bankman-Fried, founder and CEO of FTX US. The hearing addressed concerns over the gaps in the current regulatory environment for digital assets in the U.S. Chairman Behnam explained the current regulatory landscape and urged Congress to expand the CFTC's jurisdiction and resources to regulate the market structure for digital assets. All panelists and Senators present were amendable to the CFTC assuming some jurisdiction over the digital asset spot market. The hearing came after leaders of the Senate and House Agriculture Committees sent a letter to Chairman Behnam inquiring about the CFTC's role overseeing digital assets.

On February 15, 2022, the Senate Banking Committee held a hearing entitled, "Examining the President's Working Group on Financial Markets Report on Stablecoins", where Under Secretary Nellie Liang was again the only witness. Liang stated that her goals for the crypto industry include ensuring it is not used for illicit finance, promoting financial inclusion, and addressing risks related to consumer protection and financial stability. Liang argued that although the Financial Stability Oversight Council (FSOC) would have the tools to monitor stablecoins, it could not act as a substitute to Congressional action. Senators from both parties urged bipartisanship on stablecoin regulation multiple times; however, the partisan divide over stablecoins remained as Chairman Sherrod Brown (D-OH) and Sen. Elizabeth Warren (D-MA) heavily criticizing the digital asset class while Ranking Member Pat Toomey (R-PA) was more supportive of the industry.

Treasury Department

Treasury Assistant Secretary for Legislative Affairs Jonathan Davidson sent a letter to a bipartisan group of Senators on February 11, signaling that crypto-miners and stakers will not be subject to tax reporting requirements passed in last year's Infrastructure Investment in Jobs Act. According to the industry, certain groups, such as miners and stakers, do not have access to that kind of information, which makes compliance difficult -- if not impossible -- if they are included. Sen. Pat Toomey (R-PA), ranking member of the Senate Banking Committee, said he was encouraged by Treasury's letter. However, he still wants lawmakers to pass legislation codifying the clarifications. The Treasury Department has until 2023 to finalize any ruling on the tax provision.

In a recent study, the Treasury Department emphasized the potential for nonfungible tokens (NFTs) to be used for illicit money laundering and terror financing. The study illustrates the importance of NFTs in representing ownership of digital and physical property that can be controlled and managed via smart contracts and digital wallets. Treasury further notes that the price of NFTs is determined by the buyer and seller and not by the market. The study was the first time an agency has substantially discussed NFTs, signaling that other regulatory agencies and Congress may be interested in the topic in the future.

Securities and Exchange Commission (SEC)

The Securities and Exchange Commission (SEC) has proposed a rule that could bring more digital asset exchanges under its jurisdiction. The amended rule seeks to fill a regulatory gap by making platforms sitting outside the SEC's supervision comply with existing standards intended to protect investors and promote fair and orderly markets. While the new 654-page guidance, backed by the SEC last month, does not explicitly reference digital asset exchanges, experts in the crypto sector, legal experts, and SEC commissioner Hester Pierce believe the industry could fall under an expanded SEC "exchange definition" that is meant to capture platforms trading securities outside the agency's jurisdiction. The rule is open for public comment for 30 days.

During a recent Politico interview, Valerie Szczepanik, the head of SEC's strategic hub for innovation and financial technology, said the exposure of regulated financial institutions to cryptocurrency trading, as well as related activities such as lending and collateralization, increases financial stability risks. She expressed particular concern regarding DeFi platforms, an issue the SEC has been monitoring more closely in recent months.

The SEC recently levied its largest penalty against the crypto industry, a $100 million fine against crypto startup BlockFi. BlockFi was accused by the SEC of defrauding investors over the last three years by selling unlicensed investment products worth billions of dollars. As part of the settlement, BlockFi agreed not to open any new lending accounts to U.S. customers and register a new investment company, BlockFi Yield, as an SEC-registered investment company. SEC officials stated that the penalty would have been higher if the company had not cooperated with the investigation. SEC Chair Gary Gensler stated that the settlement demonstrated the SEC's willingness to work with crypto companies. He said that the settlement demonstrated that crypto markets must comply with "time-tested securities laws, such as the Securities Act of 1933 and the Investment Company Act of 1940."

Federal Deposit Insurance Corporation (FDIC)

The Federal Deposit Insurance Corporation (FDIC) has said that crypto—and specifically the risks involved in the crypto industry—will be a priority area of focus for 2022. Newly appointed FDIC Acting Chairman Martin “Marty” Gruenberg stated that crypto asset products could pose "significant safety and soundness and financial system risks." The FDIC's focus on crypto-related risks follows similar actions by other regulatory agencies.

Federal Bureau of Investigation (FBI)

The Federal Bureau of Investigation (FBI) has launched a team to investigate crimes involving cryptocurrencies. The National Cryptocurrency Enforcement Team (NCET) will assess which types of cryptocurrency-related crimes require additional resources to investigate and prosecute. Ransomware will be a key focus of the team as other agencies and Congress have raised alarms over the use of cryptocurrency as ransomware in cyberattacks.

State and City Updates (Colorado)

Colorado will accept cryptocurrencies for tax and other payments to the state by the end of the summer, Governor Jared Polis said during an interview. Polis stated that the move was for consumer convenience and that crypto should be accepted at the same level credit cards are accepted. Polis has a long pro-crypto history after becoming one of the first U.S. politicians to accept bitcoin as campaign contributions when he ran for Congress in 2014. Colorado wouldn't be the first state to accept taxes via digital assets, but pilot programs in Ohio and Seminole County, Florida, were ultimately unsuccessful and scrapped.

Looking Ahead

TBD	• White House Executive Order

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