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. The Policy Notes on Decentralised Finance and Decentralised Autonomus Organisations are published, the report on non-fungible tokens is being finalised. 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. The election of the chairs has been completed, and delegated leadership for the SubWGs has been initiated. 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 18th February until 04th March 2022.

In Brussels, legislative activities have undergone a sharp change in the last week due to the terrible events in Ukraine, following the invasion by the Russian Federation. In the week prior to the invasion the new version of the European Parliament's MiCA compromise amendments was circulated and the Commission presented its proposal for a Data Act. Crypto assets are featuring high on the agenda of European regulators, due to the perceived risks for Money Laundering following the economic sanctions on Russia.

Regulation of the crypto industry, outside of its impact on sanctions, will take a back seat in the coming weeks as Congress and the Biden Administration are laser-focused on the Russia-Ukraine conflict. Some had speculated that the State of the Union (SOTU) address could have been a forum for President Joe Biden to mention crypto, signaling it as a priority of his administration, but that did not happen. In non-sanction-related news, the Securities and Exchange Commission (SEC) launched an inquiry to determine if non-fungible tokens (NFTs) are used to raise money like traditional securities. This will be the first time a US regulator has taken action on NFTs.

EU Policy Developments

Markets in Crypto Assets: New Compromise Amendments

On 28 February, the new version of the compromise amendments from the European Parliament on the Markets in Crypto Assets Regulation (MiCA) was seen. This new version removes the changes proposed by the Members of the European Parliament from the Green political group, that introduced an environmental sustainability standard on the crypto asset consensus mechanism, the so-called proof of work. The changes on the environmental standards received significant backlash as they would've implied a ban on Bitcoin. Additionally, this new version of the text introduces changes to the thresholds of significant asset referenced tokens (ARTs), raising further the criteria for determining whether an ART is significant, meaning any ART below the thresholds are not deemed significant. The limits which have been doubled for each criterium are now (I) a customer base of 20 million natural or legal persons, (II) a market capitalisation of EUR 10 billion, (III) per day transactions of 5 million or of a value of EUR 1 billion or (IV) the size of the reserve assets shall be EUR 10 billion.

The vote on the compromise text was expected for 28th February however after the backlash the previous compromise text received, the vote was cancelled. The expectation is now that a new ECON vote will take place in the next few weeks, pending an agreement with the shadow rapporteurs.

Data Act: Proposal by the European Commission

On 23 February 2022, the European Commission presented its Proposal for a Regulation on harmonised rules on fair access to and use of data (Data Act). It is a major milestone in the Commission's overall 2018 Data Strategy, aimed at unlocking the potential of data and incentivising businesses and governments to share data more widely across the continent. The Data Act contains rules for data sharing (B2B, B2C and B2G), access by public bodies, safeguards for international data transfers and interoperability obligations. It also introduces a right of users to access and share the data generated using products or related services. It applies to manufacturers, data holders, data recipients, public sector bodies, and providers of data processing services offering such services to customers in the EU. For the financial services sector, the upcoming Open Finance framework the EC is currently working on (proposal expected in 2022) will build on and be in full alignment with the principles of the Data Act. While the revised Payment Service Providers Directive (PSD2) opened up the sharing of data on payments accounts and introduced open banking, allowing third party providers to create new services, the open finance framework will seek to extend this and enable B2B/B2C data sharing in broader financial services areas. The new rules will set the framework that would allow for consumers to share their financial data with third parties.

Crypto-Assets: FSB comments on financial stability

The FSB published its assessment of "Risks to Financial Stability from Crypto-assets". The report examines developments and associated vulnerabilities relating to three segments of the crypto-asset markets: unbacked crypto-assets (such as Bitcoin), stablecoins, and decentralised finance (DeFi) and other platforms on which crypto-assets trade. In particular, the report highlights that although the direct connections between crypto-assets and systemically important financial institutions/core financial markets are limited at the present time, the current trajectory could have implications for global financial stability. Furthermore, a lack of transparency and concentration of risk exists due to a relatively small number of crypto-asset trading platforms aggregating multiple types of services and activities, including lending and custody. In addition, the report also highlights liquidity concerns within the broader crypto-asset ecosystem (including DeFi) where a major stablecoin fails. This would disrupt trading and potentially cause stress in the wider markets. The report finds that although the extent and nature of the use of crypto-assets vary somewhat across jurisdictions, financial stability risks could rapidly escalate, underscoring the need for timely and pre-emptive evaluation of possible policy responses.

Crypto-Assets: EU plans following sanctions on Russia

EU finance ministers agreed that new measures are needed to ensure that Russians don't use cryptocurrencies to evade international sanctions. During an informal video call, ministers agreed to crack down on crypto as they took stock of the economic fallout that could come from Russia's invasion of Ukraine. In addition, the European Commission is preparing a package of measures for the week of 7 March that will also help countries cushion the impact the war will have. More details on the crypto measures will likely be alongside that package.

"There is an increased volume of transactions in cryptocurrencies and crypto-assets" that could suggest that the market is being used to "evade sanctions," Executive Vice President Valdis Dombrovskis reported after the video call. The value of Bitcoin has increased in recent days, reinstating fears that sanctions taken by Western countries — including freezing bank assets and cutting off the Central Bank of Russia — could be somewhat avoided.

Looking Ahead

7 March 2022	• Coreper II

8 March 2022	• Working Party on Financial Counsellors
9 March 2022	• Coreper II
10 March 2022	• Informal meeting of Heads of State or Government
11 March 2022	• Informal meeting of Heads of State or Government
14 March 2022	• Eurogroup
15 March 2022	• Economic and Financial Affairs Council
16 March 2022	• Coreper II
16 March 2022	• Financial Services Committee
18 March 2022	• Coreper II

US Policy Developments

Sanctions

As the US, EU, and other bodies and nations impose sanctions against Russia, there have been reports about the potential for cryptocurrency to be used as tools to circumvent sanctions. The Wall Street Journal reports that the Biden administration is now considering adding cryptocurrency to sanctions talks, citing an administration official. The official said sanctions on Russia's crypto activities would need to be crafted in a way that would not destroy the broader crypto market, making imposing them difficult. Treasury officials noted that the risk of crypto to circumvent sanctions was low since washing large quantities of any asset is extremely costly and would move markets. Todd Conklin, counselor to the deputy Treasury secretary, said in an interview last week that, “the scale of what they have to move, and where they have to move things from, [crypto's] not necessarily going to be that concerning."

To date, crypto is not explicitly part of any US sanctions measures. On February 28, news reports indicated the Biden administration is applying pressure on crypto exchanges to ensure Russian individuals and organizations are unable to avoid sanctions. Led by the National Security Council and the Treasury Department, the administration is reportedly working with Binance, FTX, and Coinbase. The exchanges deny blocking all Russian users but are working with the administration to ensure compliance with sanctions.

Congress

In a letter sent to Treasury Secretary Janet Yellen, four Senators, including Senate Banking Chairman Sherrod Brown (D-OH) and Senator Elizabeth Warren (D-MA), expressed concern that the cryptocurrency industry may not be complying with U.S. sanctions. The letter also expressed concern that the Treasury Department's Office of Foreign Assets Control (OFAC) did not provide sufficient and effective enforcement for the crypto industry. Additionally, the letter asked if decentralized financial (DeFi) structures operating without intermediaries impede sanctions enforcement. Senators, including Sen. Warren, have been raising concerns that Russia is trying to evade sanctions by using crypto. The senators asked Secretary Yellen to respond to their questions by March 23.

Treasury Department

The Treasury Department's Office of Foreign Assets Control (OFAC) solidified a Russia-related executive order the Biden Administration issued last year by issuing new rules on transacting with Russian entities. The order listed "deceptive or structured transactions or dealings to circumvent United States sanctions, including through the use of digital currencies or assets or through the use of physical assets," among its prohibited activities. The rule took effect on March 2 when it was published in the Federal Register. Because the regulations pertain to an executive order relating to a national emergency, the usual procedure of proposed rulemaking and comment period does not apply. The rules do not specifically mention crypto assets but reiterate the executive order, which prohibits digital transactions that circumvent the rules.

On March 1, 2022, the Treasury Department published the National Risk Assessments for Money Laundering (NRAs) for 2022. The report highlights the greatest threats to illicit finance and notes that crypto's use in illicit finance is lower than fiat currency and more traditional methods. Crypto was, however, increasingly used in illicit activities, including evading sanctions. Additionally, the report noted the use of crypto in cyberattacks.

Securities and Exchange Commission (SEC)

The enforcement director of the Securities and Exchange Commission (SEC) said that the SEC would not offer amnesty to cryptocurrency companies that self-report violations of securities laws, although they may face smaller penalties. Director Gurbir Grewal's first remarks on crypto clarify SEC enforcement policy moving forward and show that while the agency may be more lenient towards those who engage and self-report, they will still be subject to penalties. Many in the industry expected the SEC to offer a self-reporting amnesty. Still, Grewal's comments disappointed those in the industry who have argued for one-time passes until more regulatory clarity has been provided. Grewal assured companies that the SEC would be more friendly to self-reporting companies. Grewal's comments come after SEC Chairman Gary Gensler called for crypto companies to engage with the agency.

A speech by SEC Chairman Gary Gensler at a Democratic Party retreat focused primarily on crypto. During his speech on financial services priorities, he reaffirmed that the SEC has legal authority over more of the market than is currently acknowledged. Gensler compared the high level of crypto ads during the Super Bowl to the subprime mortgage boom that led to the financial crisis of 2007-2008, a criticism also made by Senate Banking Chairman Sherrod Brown (D-OH) last month.

The SEC is examining non-fungible token (NFT) creators and crypto exchanges trading NFTs to see if some of the assets fall within the SEC's jurisdiction. The probe is set to determine if NFTs are being used to raise money like traditional securities. Attorneys at the SEC's enforcement division have already sent subpoenas asking for information about the token offerings. In addition, the SEC is looking for details about fractional NFTs, which involve breaking down assets into units that can be easily bought and sold. The inquiry represents the latest effort by Chairman Gensler to ensure the crypto market complies with its regulations, asserting that the majority of digital assets fit the Howey test for securities and are therefore under the SEC's jurisdiction. While this is the first U.S. regulatory action on NFTs, SEC Commissioner Hester Peirce recently hinted some NFTs are under SEC jurisdiction and called for the SEC to be a leader on the asset class.

Federal Reserve (Fed)

In a speech at the US Monetary Policy Forum, Federal Reserve Governor Lael Brainard emphasized the importance of the US being on the frontier of research and policy development regarding a central bank digital currency (CBDC). Her remarks stressed the importance of keeping up with the changing financial system so the US currency continues to be strong and safe. Brainard is one of the biggest advocates of a Fed-issued CBDC at the Federal Reserve and will likely push for movement on the topic more when confirmed as Vice Chair.

The new Federal Reserve investment and trading activity rules prohibit senior Federal Reserve officials from purchasing stocks, bonds, agency securities, foreign currencies, commodities, sector funds, and cryptocurrencies. Crypto originally was not included in the banned purchases in October but was added in late February. For now, the regulations apply only to senior Fed officials. The new policy takes place on May 1 and was enacted in response to reports of active trading in a wide range of securities by several top Fed officials that resulted in the firing of two top officials. During the House Financial Services Committee, "Monetary Policy and the State of the Economy," Chairman Pro Tempore of the Federal Reserve System, Jerome "Jay" Powell, mentioned crypto concerning the financial sanctions imposed on Russia. In a rare statement on legislation, Powell called on Congress to pass legislation that prevents cryptocurrencies from being used for illicit purposes. Powell also argued that a Fed-issued central bank digital currency (CBDC) would not stop the emergence of private stablecoins.

State and City Updates (Colorado)

The US states of Georgia and Illinois are both considering tax incentives for cryptocurrency mining. While the issue of bitcoin mining's energy consumption has been brought up on the federal level, both states are considering tax breaks for bitcoin mining; joining Texas and Kentucky currently offer similar incentives to draw miners to their states.

Looking Ahead

28 March 2022	• House Financial Services Committee hearing, "The Future of Money: Assessing the Benefits and Risks of a U.S. Central Bank Digital Currency"
TBD	• White House Executive Order

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