

## Developments in the Regulation of Crypto-Assets – 2022 Update

### EU Regulation of Crypto-Assets

The increased prevalence of investment in crypto-assets has prompted European regulators to propose a legal framework to streamline the regulation of such assets throughout the EU. The Markets in Crypto-Assets Regulation (“MiCA”) is a proposed regulation in EU law which is due to be formally adopted in legislation in 2024. MiCA was created by the European Commission to ensure EU consumers can gain safe exposure to innovative crypto-assets without creating challenges to market stability.

The main objectives of MiCA are as follows:

- To provide legal certainty for crypto-assets not covered by existing EU financial services legislation.
- To establish uniform rules for crypto-asset service providers and issuers at EU level. Crypto-asset service providers include activities such as:
  - The custody and administration of these assets.
  - The operation of a trading platform for these assets.
  - The exchange of crypto-assets for fiat currency.
  - The execution of orders for these assets and the provision of advice on crypto-assets.
- To replace existing national frameworks applicable to crypto-assets which are not covered by existing EU financial services legislation.
- To establish specific rules for so-called “stablecoins” or e-money. Stablecoin is any cryptocurrency which is designed to be pegged to a commodity or currency.

MiCA also introduces a number of crypto-asset definitions. These include the following:

- Crypto-assets: digital representation of value or rights which may be transferred and stored electronically using distributed ledger or similar technology.
- Distributed Ledger Technology (“DLT”): a type of technology that supports the distributed recording of encrypted data.
- Utility Token: a type of crypto-asset which is intended to provide digital access to a good or service, available on DLT, and is only accepted by the issuer of that token.
- E-money Token: a type of crypto-asset the main purpose of which is to be used as a means of exchange and that purports to maintain a stable value by referring to the value of a fiat currency that is legal tender.
- Crypto-asset Service Provider: any person whose occupation or business is the provision of one or more crypto-asset services to third parties on a professional basis. Examples of such service providers are included above.

### Developments in Ireland in 2022

Before MiCA comes into force, crypto-assets currently have no regulatory framework in Ireland. However, there are no rules which specifically prohibit any activities related to crypto-assets. It should also be noted that such assets are neither guaranteed nor regulated by the Central Bank of Ireland (“CBI”). The CBI has recently issued warnings to consumers about the risks/dangers of investing in these assets such as extreme volatility, absence of regulatory protection and risk of total loss.

The CBI recently commented on the increase in enquires it has seen in relation to crypto-assets. In early 2022, the CBI issued guidance on crypto-assets in its Securities Markets Risks Outlook Report. The CBI made the following observation:

*“At the moment, while such assets may be suitable for wholesale or professional investors, the CBI is highly unlikely to approve a UCITS or a Retail Investor AIF proposing any exposure (either direct or indirect) to crypto-assets, taking into*

*account the specific risks attached to crypto-assets and the possibility that appropriate risk assessment could be difficult for a retail investor without a high degree of expertise.”*

The CBI has made it clear that exposure to crypto-assets will only be via QIAIFs which are targeted at professional investors with a minimum subscription amount of €100,000. The CBI has also stated that where a QIAIF is seeking to gain exposure to crypto-assets, the Alternative Investment Fund Manager (“AIFM”) is required to demonstrate that it can effectively manage the risks posed by crypto-assets exposure.

In Q1 2022, the CBI approved, in principle, two QIAIFs to gain indirect crypto-asset exposure. The two QIAIFs were approved to gain a low level of exposure to cash settled Bitcoin (a digital currency) futures traded on the Chicago Mercantile Exchange (“CME”). The CME is a US-registered derivatives clearing organisation and is the world’s largest financial derivatives exchange. A spokesperson for the CBI clarified that the futures in these QIAIFs do not involve an exchange of physical bitcoins and that the indirect crypto exposure is not the predominant focus of these QIAIFs’ investment strategy. It was also noted that the indirect crypto exposure is limited to a small proportion of net assets.

This is the first time the CBI has approved indirect exposure to crypto-assets for a QIAIF. It is understood that there are a number of other similar applications with the CBI which they are considering. The increased demand for funds with crypto-asset exposure is being driven by institutional investors seeking exposure to it as an asset class.

### **Recent Developments in Other European Countries**

Germany is currently leading the way in Europe and made crypto-assets official financial instruments in 2020. Luxembourg is reportedly set to have its first AIF investing exclusively in crypto-assets in Q2 or Q3 2022. Switzerland and Germany currently allow pure-play crypto exchange traded products.

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- The provision of UCITS management company/AIFM services.
- The provision of designated persons to perform UCITS business plan/AIFMD programme of activity functions.
- The provision of operational and compliance services to both UCITS and AIFMD compliant structures.

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