

# Podcast - Beyond the Hype – the future of digital assets

Judith Bremer and Emiliano La Sala

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**Judith:** Hello everyone and welcome to our new podcast series Beyond the Hype – the Future of Digital Assets, where we will be discussing all types of questions in the current regulatory landscape for digital assets, with experts from both Allen and Overy as well as other market players. My name is Judith Bremer and I'm an associate in the financial regulatory team in Frankfurt. I am joined today for this first episode with Emiliano La Sala, counsel in our Milan office and head of Domestic Capital Market and Fintech Group coordinator. Hi Emiliano thanks for joining me.

**Emiliano:** Hi, Judith.

**Judith:** Today we will provide you with an overview of how the various legislations are designed to interact and where they may be covering distinct aspects. So Emiliano, to start off with something that has shaken the digital assets world quite a bit, with the crash of Terra USD, one of the world's largest stable coins and the bankruptcy of the leading crypto exchange FTX, it seems that there is still no clear regulated landscape for the blockchain phenomenon in order to protect investors and promote market stability. Can you tell us something more about this?

**Emiliano:** Thank you Judith. First of all, we should identify which application of the blockchain technology we are considering here. By blockchain or distributed ledger technology, we are generally referring to a technology which provides cryptographically secure distributed database, the ledger that maintains a continuously-growing list of records, called blocks, and each block contains a timestamp and a link to a previous block, and is validated by consensus among multiple computers. The chain is immutable, and data on the blockchain is not stored in any single place as it is distributed across many different nodes. As such, a DLT can be applied to any transfer of assets, not only to crypto assets such as the tokens, Terra USD or FTT. In addition, when talking about DLT, one should always bear in mind that blockchain is in reality an umbrella term for various technologies.

In my opinion, the critical element is the distinction between permissioned and permissionless blockchains. At the simplest level, the distinction lies in whether the design of the network is restricted to certain predetermined participants, or is open for anyone to join and take active part in the validation process.

**Judith:**

So when we consider blockchain, we are not only talking about cryptocurrencies such as Bitcoin or Ethereum. Is that right?

**Emiliano:**

Correct, the blockchain phenomenon is much larger than cryptos and capable multiple applications, in particular, anytime someone is requested to record the ownership of an asset and is transferred from one person to another, no matter if applied to real estate, artworks, ships or financial securities, and whether in the real world or in the metaverse.

**Judith:**

In other words, the potential use cases for blockchain evolve at breakneck speed. That makes me wonder about how legislators and regulators intend to protect participants. Apparently blockchain is largely unregulated, so can you tell us if there are any developments in this respect in the European legislation?

**Emiliano:**

Yes, you are perfectly right. For the time being, blockchain and more particularly service relying on DLT applications are mostly unregulated. However, European co-legislators have worked very hard in the last couple of years to design a harmonised and comprehensive regime designed to both incentivise an efficient digital transformation within the union, as well as ensure market stability and adequate investors protection.

In particular, in September 2020, the European Commission took the first formal step in response to the blockchain and crypto assets phenomenon by adopting the digital financial package. This package consists of three legislative proposals regarding the digital operational resilience (the so-called DORA regulation), markets in crypto-assets (the well-known MiCAR) and a pilot regime for marketing infrastructure based on DLT (the so-called Pilot regime).

In considering the application of the DLT technology, the European legislator has distinguished between, on one side, assets that can be qualified as financial instruments for which the already existing legal framework still applies, but needs to be amended to take into account the tokenised nature of such securities.

And on the other side, other crypto assets, for which a new regulatory framework is still necessary. The legislation aimed at amending the current legal framework applicable to financial instruments in tokenised form is the so-called Pilot regime and entered into force on 23 March of 2023. The new legislation on crypto assets, which are not qualified as financial instruments, the MiCA has been recently adopted by the European Parliament.

**Judith**

Coming back to the first point of the DLT Pilot regime, can you maybe tell us something more about the aim of the Pilot regime?

**Emiliano:**

Yes. The Pilot regime represents the first concrete EU legislative framework aimed at creating a regime for market infrastructure based on distributed ledger technology, and enabling such entities to benefit from

exemptions from some specific requirements of the Union financial services legislation.

In particular, upon certain conditions, the Pilot regimes allows the DLT market infrastructures to be temporarily exempted from those provisions and requirements laid down in EU's financial services legislation, including CSDR and MiFID that might prevent the application of new technologies for the trading and settlement of transaction related to financial instruments issued using DLT.

The Pilot regime is primarily addressed to multilateral trading facilities and settlement systems and, in general, to all those entities being involved with the issuance, transfer and settlement of financial instruments such as issuers, MiFiD investment firms, central depositories and central counterparties.

**Judith:** And as opposed to the Pilot regime, there is MiCAR, and as I understand it, this will cover non-financial instrument tokens. Is that correct?

**Emiliano:** Yes, the MiCAR does not apply to financial instruments, non-fungible crypto assets, including NFTs and Crypto Asset Service, providing a fully decentralised manner without any intermediary, i.e. DeFi is not in scope. Crypto-assets are classified by MiCAR as e-money tokens (EMTs), asset-referenced tokens (ARTs), and crypto assets other than asset-referenced tokens and e-money tokens.

The aim is to ensure adequate protection to investors in crypto assets, while preserving the market integrity and the stability of the financial system.

**Judith:** And thereby creating entirely new classes of regulated instruments. May we quickly run through some of the main tools on legislative requirements whereby MiCAR intends to achieve its goals?

**Emiliano:** Well, without being exhaustive, some of the key takeaways from MiCAR are the following. The MiCAR will introduce the first sole comprehensive regulatory regime addressed in the crypto space. Its provisions will regulate from many different angles matters such as licensing requirements, products taxonomy, market operator rules of conducts, disclosure requirements on issuers and market abuse requirements.

Also, the MiCAR would preserve the market and financial stability by imposing on the market operators, depending on their legal status and size, prudential and capital requirements.

**Judith:** That is understood. Thank you for this outline. Now we understand that the next episodes of this podcast will focus on MiCAR. Can you give us a brief overview of what's next?

**Emiliano:** With our next podcast, we will give an overview of several key requirements and provisions in MiCAR, including, to list just a few, its scope, issuance of

EMTs and ARTs, conditions for marketing of crypto assets, as well as an overview of the market abuse and AML regimes applicable to crypto assets. Having said that, we invite the audience to share with us any thoughts and comments that they may have in relation to MiCAR and we will try to address them in our next episodes.

**Judith:**

Thank you Emiliano and also thank you to all those who joined us today. We are looking forward to hearing from you, your thoughts and questions, and discussing them in more detail in the episodes to come.

Stay tuned.