Hogan Lovells / GBBC Digital Finance Digital Asset and Blockchain Dinners: Dublin

With the MiCA now published in the Official Journals; trilogues on the EU's Anti-Money Laundering Regulation commencing; and a race to get the level 2 part of DORA finalised in time for the 17 January 2025, it was a timely occasion to host the next edition of the Hogan Lovells / GBBC Digital Finance, Digital Assets and Blockchain Roundtable Dinner series. This time in Dublin.

The focus of the discussion was the EU's digital finance strategy, with members of industry, both traditional finance and digital asset firms, discussing the impact this will have and what we can expect going forward.

At the time of the dinner, MiCA's publication in the Official Journals was imminent and participants discussed the impact that the regime would have. Whilst there was general optimism about having a regime for the regulation of crypto assets vs not – the US's approach of regulation by enforcement did come up, again poignant given recent actions taken out against Binance and Coinbase by the SEC – it was clear there were shortcomings.

When discussing the clarity that the MiCA regime brings, participants pointed to the fact that there are still a lot of layers that issuers will have to peel through to be able to get their token on the market. Being a subsidiary piece of legislation, firms will have to conduct analysis under existing EU financial services legislation such as MiFID and prove that it does not apply before applying MiCA which doesn't necessarily provide an easy route to market or clarity. Participants talked about the structural nightmare of having a Directive in MiFID that takes precedent over a Regulation in MiCA, meaning differing interpretations of a security across the Union provides an arbitrage opportunity.

Participants therefore highlighted that as such MiCA is not necessarily the 'bespoke' regime that it purports to be. In fact when discussions moved to the UK regime, which was consulted on earlier in the year, remarks were made as to how aligned the two in reality are.

Whilst the UK seeks to bring cryptoassets within the remit of FSMA Authorisation – in effect bringing digital assets within the remit of traditional financial services legislation – and seek to add new rules for aspects that do not quite fit or expand the perimeter to apply to certain digital assets, MiCA created a standalone set of rules.

But what does the regime look like in practice? The reality is that MiCA does the same thing, it applies existing EU financial services legislation before then applying rules from MiCA which are largely adapted from existing EU financial services legislation. So rather aligned.

Participants dug deeper into the point around both regime being largely adapted from existing financial services legislation. As discussions around MiCA level 2 text developed, comments were made around how similar much of this will be to MiFID. There was push back from some in the room who questioned why this mattered ie. whether it was treated as traditional financial services or not. This was a timely intervention given the publication from the UK's Financial Conduct Authority just a day later which mentioned that many tokens on the market were being used as substitutes to traditional financial instruments. So it raised a good question; if it is being used as a financial instrument should it not have the same treatment?

Zooming out on what was being discussed an interesting point unearthed. Whilst the US are acused of getting stuck in the discussion of whether digital assets are a security or not and trying to put everything into the definition of a security, has the EU and for that matter the UK just taken the exact same approach but packaged it up differently?

Afterall with MiCA, if MiFID doesn't apply, the MiCA rule book is relatively similar and therefore is applying slightly more proportionate securities law.

With the proposed UK regulatory regime, we have a similar situation, the existing regulatory perimeter has opened up and whilst we wait for how the regime will be applied it could very well be applying similar measures to securities law, just proportionate.

As the discussion on MiCA drew to a close, there was consensus that what mattered most from an industry perspective is the layer below regulation. Whilst jurisdictions take a similar approach or slightly varied approach, what is most important is: access to talent, finance, legal certainty and a regulatory environment and regulator that is welcoming. If there is a race to become a centre for digital assets, that will be where it will be won or lost.

This made it all the more important that the discussion was hosted in Dublin, with Ireland shaping up as a choice location for digital assets firms to headquarter themselves and passport into the EU with their MiCA license. Topical given Gemini's recent announcement of choosing to have their European Headquarters in Dublin.

The conversation then moved to the EU's anti-money laundering package. Participants acknowledged that the Transfer of Funds Regulation, one of four files within the package, was seminal, with a huge industry effort to ensure the preparedness of industry to be able to comply with this through IVMS101, which GBBC Digital Finance led.

However, it was the EU's Anti-Money Laundering Regulation that was of most interest to participants. Currently in trilogues, there was concern at the diverging views that Parliament and Council had entering the negotiating table and the concern that there was a lack of consistency in the read across from MiCA.

One participant mentioned that what does not help is the different teams negotiating the AML package and MiCA, and no cross over in discussion despite the close nexus between them. The lack of communication is evident when looking at the files. Parliament's decision to bring NFT platform providers within the scope of AMLR as an obliged entity, undermines discussions concluded in MiCA. Notwithstanding concerns around the absence of definition of what an NFT service provider is, MiCA deemed that NFTs should be reviewed in 18 months. The lack of alignment creates confusion for industry with rather punitive measures being applied on a nascent industry. Participants agreed that there needs to be a level of proportionality in order for this industry to be able to develop.

Discussions also went onto self-hosted wallets. Starting with concerns around the Parliament's almost ban, participants were still concerned that the EU are in danger of taking a prohibitive stance. Post FTX, there has been an increased movement of funds from being held on exchanges to self-hosted wallets. Contrary to the assumption that self-hosted wallets are for concealing funds, it was deemed that it is more secure and there was less risk of it being lost or stolen. As such, putting stringent obligations on institutions interacting with self-hosted wallets could price out this option or the development of this sector of the industry.

Being in Dublin, it would have been remiss of us to not talk about another significant part of the AML package, the EU's Anti-Money Laundering Authority (AMLA) a Super regulator for the EU. The closest example of what AMLA will look like is the ECB's SSM, but participants acknowledged that for AML, it is much bigger than that. As we look at the movement of EU legislation, we are seeing more and more legislation taking the form of Regulation and therefore a greater demand for supranational regualtors like AMLA. Ireland have bid to host AMLA and participants welcomed this. Discussions noted that Dublin is well placed to win this given it: is English speaking, is a common law jurisdiction, has close ties with the UK and US, has strong financial services community and narrowly missed out on the ECB (by one vote).

It was agreed that this would be a huge win for Ireland and could signify a huge influx of companies looking to move to Ireland to be closer to the regulator.

Conversation then moved to the Digital Operational Resilience Act (DORA). The importance of this was not lost on participants who noted that this is an incredibly comprehensive regulation that will have an effect across a number of industries including crypto asset services providers (CASPs) authorised under MiCA. MiCA delegated points on operational resilience to DORA. Given the substantial level of requirements in DORA, will be difficult for CASPs to comply and it should not be overlooked at how comprehensive this will be. The concern is profound with traditional firms who are highly regulated so it will certainly be of concern for new market entrants.

With a consultation coming out this summer on what constitutes a critical outsourcing and the criteria that forms this decision, industry is waiting on bated breath to find out whether they will fall into scope and therefore need to quickly gear up ahead of DORA applying from 17 January 2025.

It is clear that 2025 will see a sea change in the way in which firms are regulated and it appears that what was otherwise considered an unregulated industry will be caught by some of the heaviest and most comprehensive regulatory regimes that the EU has delivered to date.

The conversation closed on the tokenisation of real world assets. A topic that has featured in a number of discussions between Hogan Lovells and GBBC Digital and a topic that will no doubt take a headline slot at a future dinner in this series.

Whilst much of the discussion over the course of the dinner looked at regulation and the impact that this has on the digital asset industry, this part of the discussion moved to what the technology brings to transforming industry and societies.

Participants delved into the economics of tokenisation and how it opens up access to finance for firms. Tokenisation opens up a larger pool of investors who were otherwise excluded from the investment, by allowing them to invest in a smaller portion of it. But participants cautioned that whilst this is the case, it could still be dominated by traditional investors who will dominate the market.

But the benefit is that it also presents the ability to make otherwise illiquid markets liquid. The example was given of the housing market. For example. tokenisation allows for the partial purchase of a house. This mean that in a situation whereby an investor was precluded from buying a house as an investment as a result of not having sufficient funds to buy it in its entirety, they are now able to due to the house being tokenised. It also benefits from the holder of the asset too, allowing them to have a more liquid market to trade their asset it. Again, there was push back from participants of the discussion who noted that culturally this was quite difficult with some people who are used to an want to own the entirety of an asset rather than a portion – a hurdle that no doubt will need to be overcome if there is going to be widespread adoption.

The use case in capital markets came up with references being made to shorter settlement times. Participants talked about how the use of DLT and atomic settlement, reduced costs and removed friction and therefore brought greater profits and benefits for the capital markets sector. However, again there was push back with some arguing that perhaps T+0 was not the ideal and that there are benefits that come with the frictions T+2 brings.

Concluding again on the theme of economics, the conversation took a turn to the importance of this discussion in the current climate. With interest rates rising to deal with the vast levels of inflation, and governments caught between needing to spend to improve public services but also reduce expenditure, this technology can help provide solutions. Participants agreed that technology provides a cost effective government policy and can help boost productivity and growth while reducing expenditure. A topic that will no doubt be unpicked at greater length at a future dinner.