The Role of Digital Money and Digital Assets in the Future: MiCA is coming

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Outline

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B. Demand and Supply of Digital (Crypto) Assets

C. Unwarranted Criticisms of the CBDCs

D. Three Different Approaches to Crypto Assets

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A. Differences between Digital Money and Digital (Crypto) Assets

1.

- ❑ Money issued by Central Banks (including CBDCs) has three features:

   a) store of value

   b) unit of account

   c) means of exchange

- ❑ Moneys issued by commercial banks have the same three features. However, they are not legal tender (people cannot be obliged to accept them). The law confers legal tender status only to money issued by Central Banks.

A. Differences between Digital Money and Digital (Crypto) Assets (Continued)

1.

- Money issued by private actors other than commercial banks (crypto issuers, technological platforms) has none of the above features (except as a limited means of exchange within the issuing technological platform).

- Implication: crypto assets and money issued by technological platforms must not be confused by users with official money.

A. Differences between Digital Money and Digital (Crypto) Assets (continued)

2.

- Money issued by Central Banks (including CBDCs) is fully guaranteed by the issuing Central Bank.

- In the unlikely event of a Central Bank's bankruptcy, money continues to be guaranteed by the Ministry of Finance of that country, based on its right to raise taxes in the future.

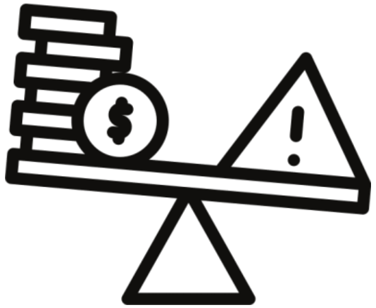
A. Differences between Digital Money and Digital (Crypto) Assets

2.

- Money issued by private actors is guaranteed by no one. Stablecoins are an intermediate case, where the issuer is free-riding on the guarantee of the Central Bank.

- The owner of the crypto assets and/or of technological platforms money bears all the risk.

- Implication: users of crypto assets must know that they have no claim on the official financial sector.



A. Differences between Digital Money and Digital (Crypto) Assets (continued)

3.
- Moneys issued by Central Banks (including CBDCs) and by commercial banks are issued "out of thin air", but always against an IOU (promissory note, treasury paper, municipal bonds, corporate bonds, paper showing future streams of income etc.). They are <u>not a gift</u>.

- Private actors are sometimes presenting money issued by them as a gift, thus luring naive customers.

- Implication: official money are a proof of the <u>creditworthiness</u> (past or future) of its holder; private actors' money are not such a proof.

B. Demand and Supply of Digital (Crypto) Assets

1.

Demand for Digital (Crypto) Assets originated with:

The criminal sector/shadow economy	Technologically-savvy, but financially ignorant, people	Libertarians, who want to have nothing to do with the state.

Later on, demand has spread to millions of youngsters who want to get rich without any effort. This is facilitated by the culture of entitlement in which we currently live.

Implication: all of the above persons tend to think about crypto assets as a substitute for money, which they are not.

B. Demand and Supply of Digital (Crypto) Assets (continued)

2.

- <u>Supply</u> of Digital (Crypto) Assets is provided by:
  - crypto issuers
  - technological platforms

- The latter have a commercial interest in controlling the private lives/tastes of their customers.
  Privately issued “money” can infringe on the personal freedom of citizens.

- Implication: The Central Banks felt compelled to issue their own CBDCs, giving people an alternative to digital (crypto) assets. CBDCs are intended to save people from themselves (naïveté, greed, ignorance). However, CBDCs cannot (and should not) make people rich overnight.

C. Unwarranted Criticisms of the CBDCs

- A lot of conspiracy theories, part of the cultural war, are accusing the CBDCs (and the Central Banks) precisely of the evils they are trying to cure: controlling the life of citizens, confiscating owners' wealth etc.

C. Unwarranted Criticisms of the CBDCs

- Against this background, the OEDC has recently published a report, “Central Banks’ Digital Currencies (CBDCs) and Democratic Values”, trying to answer these (unwarranted) criticisms. It stipulates, inter alia, that:

CBDCs must
- be designed in a way that preserve civil liberties and human rights (unlike crypto-assets). However, this must be balanced against another public goal, namely preventing money laundering and terrorism financing.

CBDCs should
- be a complement (and not a substitute) to physical money, allowing less technologically-savvy persons to carry on with their usual lives.

CBDCs should
- be resilient to security problems (cyber attacks), especially in an environment of hybrid warfare, like today.

C. Unwarranted Criticisms of the CBDCs (continued)

- However, the widespread use of CBDCs in the future might be hampered by problems such as:
  - affordability: the cost of using CBDCs might be relatively high, because they use a two-level architecture (intermediate systems), implying the existence of a third party as a payments service provider.
  - security: CBDC systems will have more entry points than the current payments systems, making them vulnerable to threats, especially from quantum computers (which are able to break actual crypting methods).

- Implication: CBDCs might end up as a “nice to have” application, but protecting people from themselves might involve new efforts in spreading financial literacy.

D. Three Different Approaches to Crypto Assets

1.

- China has officially banned crypto assets trading since 2019, seeing it as a volatile, speculative investment (at best) and a way to launder money (at worst).
- In May 2021, Chinese state institutions warned buyers they would have no protection for continuing to trade Bitcoin and crypto assets online (through foreign exchanges).
- In June 2021, they told banks and payment platforms to stop facilitating transactions and issued bans on mining the crypto assets.
- Implication: both demand and supply of crypto assets have been strongly discouraged in China. It could not afford to let a financially illiterate public to lay claims on the official sector for losses occurring from personal risky bets.

D. Three Different Approaches to Crypto Assets (continued)

2.

- The US have so far (under a Democrat administration) limited the use of crypto assets, allowing them to be traded on the Stock Exchange, but subjecting them to strict regulation by the Securities and Exchange Commission (SEC) and by the Commodity Futures Trading Commission (CFTC).
- This approach has resulted into huge fines (and CEOs detentions) for companies such as Binance or FTX.
- Implication: Since the American public generally understands risks and has no claims on the official sector for losses occurring from personal risky bets, trading of crypto assets is allowed on the Stock Exchange. Everybody understands that "who owns the asset, owns the risk".

D. Three Different Approaches to Crypto Assets (continued)

3.

<u>Europe</u> has adopted the most paternalistic (and risky) approach to crypto assets. Instead of banning them (like China) or regulating them on the stock exchanges (like the US), Europe has embarked on a widespread regulation through MiCA (Markets in Crypto Assets)

The European Commission adopted MiCA, which became law in June 2023, with an implementation planned until December 2024, when all the seven titles (chapters) will be operational.

According to the European definition, crypto assets are: asset-referenced tokens,
e-money tokens, and crypto assets other than the previous two.

Markets in Crypto-Assets Regulation (MiCA)

Implementation timeline

Last updated: 9 June 2023

June 2023
MiCA Publication in the OJEU

July 2023
Consultation Package 1 publication

October 2023
Consultation Package 2 publication

2023

Q1 2024
Consultation Package 3 publication

June 2024
Entry into application Title III and Title IV

December 2024
Entry into application Titles I, II, V, VI, VII

2024

D. Three Different Approaches to Crypto Assets (continued)

- The European Union legislation tries to regulate every aspect of the crypto assets markets: electronic wallets, “electronic money”, how “e-money” can be issued and redeemed, the liabilities of “e-money” issuers etc.

  All these regulations give the owners of crypto assets a false sense of security (which they should not have). Potentially, this approach could backfire, if the losses occurring from personal risky bets might be attributed to incomplete/ineffective regulations, thus laying claims on the official financial sector.

D. Three Different Approaches to Crypto Assets (continued)

- Moreover, MiCA leaves a lot of grey areas, with a potential for legal litigation. For example, several blockchain-related assets are not considered crypto assets:

  - crypto assets that fall under the scope of financial instruments.
  - assets that qualify as funds.
  - crypto assets that qualify as non-life or life insurance.
  - non-fractionalized non-fungible tokens etc.

E. Conclusions

Instead of making clear the huge differences between official money and crypto assets, the European legislation blurs the differences and thus exposes the official financial sector to potential claims by owners of crypto assets. This risk does not exist neither in China nor in the USA.

Due to this confusion, the European public might not perceive the difference between CBDCs (official money issued to prevent laundering, to preserve private life etc.) and crypto assets (which have the opposite goals).

A further huge mistake would be to offer CBDCs to citizens as a gift (thus obliterating their meaning as official money, issued in exchange of an IOU). CBDCs should land in the pockets of citizens as a partial substitute, not as a complement of their money holdings.

Thank you!

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