Regulation of crypto-assets in Czech Republic and the upcoming MiCA regulation

Current legislation

Although crypto-assets have become a phenomenon on the global financial market in recent years, the Czech legal system has not regulated them in any way for a long time, and even today they are only subject to a minimal regulation. The only exception were investment instruments in the form of derivatives linked to crypto-assets, which are subject to the regulation under the Capital Market Undertakings Act.

The first references to crypto-assets (originally virtual currency and later extended to virtual assets) appeared only in 2017 in the Act on Certain Measures against the Legalization of Proceeds from Crime and Terrorist Financing, according to which persons providing services related to virtual currency or assets were classified as obliged persons, as a result of which customers of these persons began to be subject mainly to identification (KYC) and due diligence requirements and trading with crypto-assets ceased to be completely anonymous. In the same year, the Value Added Tax Act also took note of the existence of virtual currency.

Since 1 January 2021, the provision of services related to virtual assets has become a separate field of activity within the scope of the free trade, which can only be performed if specifically notified within the scope of the free trade; provided that the performance of which by a legal person requires the criminal integrity of its beneficial owner and persons who are members of its statutory body.

Upcoming MiCA Regulation

However, the developing crypto-assets market requires more extensive regulation, which some countries have already attempted. Discussions at EU level have resulted in the development of unified rules for the issuance and trading of crypto-assets, and that is in the form of a proposal for a Regulation on Markets in Crypto-assets, known as the MiCA Regulation.

The draft MiCA Regulation was presented in September 2020. During the Czech Presidency of the EU Council in October 2022, a final agreement on the text of the Regulation was reached, but it still needs to be translated into all Member States' languages and then formally approved. It is expected that the Regulation could be promulgated in the first quarter of 2023, with applicability expected to be around the third quarter of 2024. Some of key innovations that this regulation of crypto-assets will bring are described below.

Requirements for crypto-assets service providers

The MiCA Regulation will only allow crypto-asset services to be provided by legal persons established in an EU Member State, based on an authorization by the competent Member State regulator; provided that such services may be provided throughout the EU through the right of establishment (including through a branch) or through the freedom to provide services (on a cross-border basis). The Regulation imposes a number of obligations on providers of crypto-assets services and introduces prudential requirements, including capital requirements depending on the type of services provided. Acquisition by crypto-asset services providers or participation in such providers will be subject to notification obligation and possibly also to approval by a home state authority.

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This will create a new category of regulated financial institutions in the Czech Republic. However, existing service providers will be allowed to provide crypto-asset services under the existing rules for a transitional period of 18 months, but after the end of the transitional period they will only be allowed to provide crypto-asset services with a new authorization according to the MiCA.

Categories of crypto-assets

The MiCA regulation does not only regulate commonly known cryptocurrencies, but distinguishes the following 3 categories of crypto-assets that will be subject to different levels of regulation:

- asset-referenced tokens, also referred to as "ART", which aim to maintain a stable value by referring to the value of several fiat currencies that are legal tenders, one or several commodities or one or several crypto-assets, or a combination of such assets;
- electronic money tokens, also referred to as "EMT", which are intended to be used as means of exchange and that purports to maintain a stable value by referring to the value of fiat currency that is a legal tender;
- other crypto-assets that are considered a digital representation of value or rights that can be transferred and stored electronically using distributed ledger technology, also referred to as "DLT", or similar technology, and that correspond to so-called utility tokens designed to provide digital access to goods or service accepted only by the issuer of these tokens.

Most traditional cryptocurrencies such as Bitcoin or Ether fall into the category of other crypto-assets. Given their non-financial nature, this category of crypto-assets is not regulated very strictly; in order to offer these crypto-assets to the public, the issuer only has to comply with basic obligations and prepare an information document called white paper, containing the information specified in the Regulation, which must be notified to the competent authority and published, and which could be considered as a kind of equivalent to a securities prospectus. A white paper will not be required if crypto-assets are offered free of charge, exclusively to qualified investors, to fewer than 150 persons in a single Member State, if the total value of the consideration for the offering does not exceed EUR 1 million or equivalent in another currency or crypto-assets over a 12-month period, or if the crypto-assets are automatically created through cryptocurrency mining as a reward for DLT maintenance or transaction validation, or in case of unique crypto-assets that are not fungible with other crypto-assets.

In order to offer e-money tokens to the public, the issuer will need to be authorized as a credit institution or an electronic money institution, comply with the legal requirements applicable to electronic money institutions and prepare and notify a white paper to the competent authority and publish it. The authorisation and the white paper will not be required if the offer is only to qualified investors or where the average unused sum of e-money tokens does not exceed EUR 5 million or equivalent in another currency (unless a Member State sets a lower threshold) over a 12-month period. Additional requirements are prescribed for e-money tokens that will be classified as significant by the European Banking Authority.

The most strictly regulated category of crypto-assets will be asset-referenced tokens. In order to offer them to the public, the issuer must obtain the relevant authorization from the competent authority of the home state, unless the token offer is only to qualified investors or the average unused sum of e-money tokens does not exceed EUR 5 million or its equivalent in another currency over a 12-month period. The regulation prescribes a number of additional obligations for the issuer of asset-referenced tokens, for example, to create and maintain an asset reserve, and imposes capital requirements on them. If the European Banking Authority classifies tokens as significant, the issuer will be required to comply with additional obligations prescribed by the Regulation. Acquisitions of asset-referenced token issuers or

participations in such issuers will also be subject to notification obligation and possibly also to an approval by the home state authority.

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