

HOW CAN LAW COPE WITH INNOVATION?

A case study of France and its reform
of crypto-assets

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Reconciling law with innovation is often a challenge for legislators since, by definition, innovation departs from existing standards and frameworks. Some may therefore question the ability of the law to address innovative trends.

However, the reform about to be finalised in France, known as the PACTE draft bill¹, includes provisions on crypto-assets and the token economy, which go against this common statement. Quite the contrary. This bill illustrates how regulators can innovate through law to support innovation.

◆ In what way is this reform innovative for the crypto economy?

The objective of the PACTE draft bill is to establish in France a regulatory framework for the crypto economy that is both attractive and comprehensive.

ATTRACTIVE

Because it strikes an original balance between

- (i) maintaining enough flexibility to support innovation,
- (ii) defining credible rules to facilitate interaction of this new economy with incumbent players (such as banks and institutional investors).

The new regime would indeed mainly provide for optional regulatory requirements, leaving it up to the market players to decide whether to opt for the regime.

COMPREHENSIVE

Because it addresses the entire crypto-ecosystem, based on the conviction that regulating both the primary and secondary markets of utility tokens is key in the efficiency of the future regime.

It includes regulatory provisions for (i) issuers of utility tokens, (ii) service providers on these utility tokens, (iii) investment funds likely to invest in utility tokens, and lastly (iv) credit institutions to ensure that the said issuers and service providers have access to banking services.

¹ Projet de loi relatif à la croissance et la transformation des entreprises

◆◆ What will change for utility token issuers?

The PACTE draft bill aims to introduce into French law **the possibility for utility token issuers to obtain a visa** for their tokens' issuance.

For the purpose of this reform, utility tokens shall be understood as digital goods giving rise to one or more rights and which may be issued, registered, stored or transferred via distributed ledger technology². The tokens, which qualify as financial instruments pursuant to MiFID II, are excluded from the scope of this regime.

This visa would be delivered by the French public authority supervising financial markets (the *Autorité des marchés financiers*, or AMF), if the offer and its issuer comply with a number of requirements, including the following:

- ◆ The issuer must provide token subscribers with a **document containing all information** relevant for the public and regarding the offer and the issuer. Such information, together with the information in the relevant marketing documents, shall be clear, fair and not misleading.
- ◆ The issuer must be a legal person **incorporated or established in France**.
- ◆ The issuer must put in place the appropriate means to **monitor and safeguard the funds** raised following the tokens' issuance.
- ◆ The issuer must comply with the obligations provided under French law on preventing the use of the financial system for the purposes of money laundering or terrorist financing (**AML/CTF**).

The General Regulation of the AMF will specify how these requirements must be implemented. These specifications should be finalised by the end of the first semester 2019, with the first visas potentially delivered by the AMF in September 2019.

Obtaining such a visa will be optional: issuers may decide whether they seek the visa from the AMF. There will be no regulatory obligation compelling the issuer to do so. However, if an issuer does decide to obtain a visa, the requirements conditioning such visa become binding. The AMF would hence be granted the power to monitor and supervise compliance by said issuer with said obligations.

With this reform, the visa is intended as an incentive to facilitate issuers' approach of potential subscribers and other stakeholders. The legal framework is meant as a marketing tool for innovative players. The same approach is also used for service providers.

◆◆ What will change for crypto-asset service providers?

Pursuant to the reform, **crypto-asset service providers established in France may opt into an optional regime**. If they decide not to opt in, service providers established in France will still be able to run their activities without being suspected of unlawful conduct in France.

However, **if they decide to opt in, they will have to comply with all the requirements applicable under the optional regime and will be put under the authority of the AMF as licensed crypto-asset service providers** (just like utility token issuers).

In other words, as soon as a crypto-asset service provider established in France decides to opt in, all the applicable requirements pursuant to the optional regime become binding.

² The PACTE draft bill refers to « *tout bien incorporel représentant, sous forme numérique, un ou plusieurs droits pouvant être émis, inscrits, conservés ou transférés au moyen d'un dispositif d'enregistrement électronique partagé permettant d'identifier, directement ou indirectement, le propriétaire dudit bien.* » - see Article 26 of the draft bill.

At this stage, crypto-assets-related services covered by the optional regime are the following (where the services are provided in relation to crypto-assets that do not qualify as financial instruments under MiFID II):

- ◆ custodian wallet provider;
- ◆ crypto/fiat exchange provider;
- ◆ crypto/crypto exchange provider;
- ◆ crypto trading platform;
- ◆ execution of orders on crypto-assets on behalf of clients;
- ◆ crypto-asset portfolio management;
- ◆ investment advice on crypto-assets;
- ◆ underwriting of crypto-assets on a firm commitment basis;
- ◆ placing crypto-assets on a firm commitment basis; and
- ◆ placing crypto-assets without a firm commitment basis.

A decree will further define each of the services mentioned above. This decree is likely to be published by the end of 2019.

To seek a license from the AMF, crypto-asset service providers established in France must permanently fulfil the following requirements:



Maintain a professional liability insurance coverage or own funds (the amount of which will be set in the AMF General Regulation).



Have in place adequate safety and internal control mechanisms.



Have in place a resilient IT system.



Have in place a system to manage conflicts of interest.

The PACTE draft bill defines further requirements that must be fulfilled on an ongoing basis by licensed crypto-asset service providers, such as the obligation to communicate to their clients clear, accurate and not misleading information (including in marketing communications); the obligation to disclose the fee policy; the obligation to put in place an effective policy for handling complaints; etc. The PACTE draft bill also lays down specific requirements for each of the services listed above. The details of the applicable requirements will be listed in the decree.

One specific exception to the optional nature of the regime is that **certain service providers** (i.e. custodian wallet providers and crypto/fiat exchange providers) **must “register” with the AMF** and will be subject to AML/CFT requirements. In this context, registration means “declaration” and is different from licensing (which refers to the licence given by the AMF to those providers that opt-in). On this basis, the AMF will regularly publish a list of registered crypto-asset service providers. **The provision of such services will be prohibited if the providers of such services are not registered with the AMF.**

This exception on the optional nature of the regime emphasises the significance of AML/CFT for France. It follows on from the implementation in France of the 5th Directive³ on the prevention of money laundering or terrorist financing to address the specific issues of the token economy in this field.

◆ What are the other key provisions on the crypto-economy in this reform?

Two set of provisions must be highlighted.

First, **the PACTE draft bill will allow certain professional investment funds to invest in crypto-assets**, which was not possible until now in France. This proposal recognises that the development of this new economy may depend on the existence of appropriate investment vehicles capable of channelling the investments into it. Taking nevertheless into account the risks that this new category of assets may bear, the reform intends to rely on the skills and expertise of professional asset managers to manage these vehicles, the marketing of which shall be restricted to professional investors and high-net-worth individuals.

Second, the reform should address the difficulties that members of the crypto-ecosystem have encountered to date when dealing with banks. **The proposal intends to require from credit institutions that they set up objective, non-discriminatory and proportionate internal rules governing access to banking services for utility token issuers having obtained a visa, and licensed Crypto-Asset Service Providers.** The legislator thus creates a new incentive to seek the regulatory authorisations described above.



The PACTE draft bill has been under discussion at the French Parliament since June 2018. In February 2019, the French National Assembly started its second review of the last version of the proposal, for a possible enactment of the reform by the end of the first semester of 2019. It should hopefully provide interesting prospects for crypto-players throughout the world.

³ European directive 2018/843

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As the debates on the PACTE draft law are still ongoing, this article was prepared on the basis of the French Parliament's working documents, not the final law text. The information contained herein is therefore liable to change.

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