

Alert | Blockchain & Digital Assets



July 2022

MICA Regulation: The EU Parliament’s Position on ‘Proof-of-Work’ Mechanism

Go-To Guide:

- Latest negotiations on EU crypto-assets Regulation have seen the EU Parliament ECON Committee refusing to order a ban on crypto-assets using the common, but highly energy-consuming, Proof of Work consensus mechanism (PoW).
- In order to achieve a compromise between the opening of a free, fair, and safe crypto-asset venue across the EU zone and the binding environmental milestones set out in Paris Agreements, EU new draft MICAR sets forth “softer” information and reporting undertakings as to the environmental impact of their crypto-assets operations.
- Users, investors, and market players on crypto-asset in the EU Zone should consider the environmental impact of their business as an important risk factor for their operations and transactions.

The ECON Committee Approach to PoW

In the context of finalising the first draft of the Markets in Crypto-Assets Regulation (MiCAR), the European Parliament Committee on Economic and Monetary affairs (ECON Committee) was considering a ban on the crypto-assets using “Proof of Work” (PoW) as a consensus mechanism to validate their underlying transactions. Notwithstanding some of the most popular cryptocurrencies’ use of this

technology (including Bitcoin and Ethereum), EU institutional concern is mainly based on the mechanism's high energy consumption, which consumption conflicts with EU environmental goals. However, in accordance with certain market players' positions, the ECON Committee at recent meetings took a "softer" approach by generally permitting the use of PoW, subject to additional disclosure requirements to be included in relevant crypto-assets white papers.

Background: MiCAR – Where Are We Now?

MiCAR is the envisaged regulation on Markets in Crypto-Assets, first drafted in 2018 in the framework of the digital finance package. MiCAR initially was proposed in response to the remarkable increase in Bitcoin and other cryptocurrency investments to create a more investor-friendly and protective legal environment vis-à-vis the market risk attached to investments in unregulated virtual assets that fall outside the scope of MiFID and other financial services legislation regimes.

To this end, MiCAR is aimed at: (i) setting out certain harmonised definitions on the subject matter, including "crypto-asset,"¹ "asset-referenced token"² and "utility token"³; (ii) providing legal certainty for crypto-assets that do not qualify as financial instruments and therefore are not covered by the current EU financial services legislation; and (iii) establishing a common framework of binding rules on "Crypto-Asset Service Providers (CASPs)"⁴ (and relevant authorization and passporting regime) and issuers based or operating in the EU space.

The aforesaid goals ultimately are intended to remove obstacles to the establishment, and improve the functioning, of the internal market for financial services, including the current inability of the crypto-assets market players across the EU to *"fully reap the benefits of the internal market, due to a lack of both legal certainty about the regulatory treatment of crypto-assets as well as the absence of a dedicated and coherent regulatory and supervisory regime at the EU level."*⁵

MiCAR approval follows the ordinary legislative procedure set forth under Article 294 of the Treaty on the Functioning of the European Union. This means that, following the Commission's first proposal, the Council and the Parliament must ultimately approve the final MiCAR text. Following the 30 June 2022 meeting between certain representatives of the ECON Committee and the Council, the EU Parliament issued a press release⁶ announcing a provisional political arrangement on certain outstanding points, including, among others, a final position as to disclosure obligations of CASPs on the environmental and climate impact of their operations.

The above political arrangement is now reflected in an updated draft MiCAR, to be approved first by the ECON Committee, and then by the EU Parliament (following a plenary vote) and the Council. The whole

¹ "A digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology."

² "A type of crypto-asset that purports to maintain a stable value by referring to the value of several fiat currencies that are legal tender, one or several commodities or one or several crypto-assets, or a combination of such assets."

³ "A type of crypto-asset which is intended to provide digital access to a good or service, available on DLT, and is only accepted by the issuer of that token."

⁴ MiCAR defines "crypto-assets service providers (CASPs)" as *"any person whose occupation or business is the provision **of one or more crypto-asset services** to third parties on a professional basis"*, such "crypto-asset services" to include, pursuant to the same MiCAR, a wide range of activities connected to the crypto-assets environment, including among other things custody, exchange, operation of trading platforms, execution of orders, placement and advisory.

⁵ See the "Explanatory Memorandum" enclosed with the EU Commission's original MiCAR proposal.

⁶ See the [press release](#).

legislative process, and consequently MiCAR's entry into force, are currently expected to be completed in 2024.⁷

Proof of Work – a Definition and Its Environmental Impact

In Article 3(1), point (28a) of the latest draft MiCAR, the ECON Committee defines PoW as “*a consensus mechanism that requires all miners that are participants to the DLT to solve complex mathematical puzzles to validate a new transaction, adding a block to the chain and permanently and irreversibly recording a new transaction.*” In particular, PoW (i) embeds a decentralized consensus mechanism requiring members of a network to solve an arbitrary mathematical puzzle to prevent anybody from gaming the system; and (ii) processes peer-to-peer cryptocurrency transactions in a secure manner and without the need for a certification or other comfort from a trusted third-party. Bitcoin became the first cryptocurrency adopting this technology and was followed by Ethereum and other cryptocurrencies with the same objective to achieve a secure and decentralized consensus of each such transaction.

Aside from its strengths in terms of secure consensus around crypto-asset transactions, PoW brings a significant and non-sustainable environmental impact, notably in terms of an increase in electricity consumption, a growth in mining equipment, and the generation of electronic waste. For those reasons, a massive application of this technology, if permitted by the EU legislation and not challenged by other more environmentally friendly consensus mechanisms, ultimately may undermine the EU mission to meet the climate and sustainability goals set out under the Paris Agreement (see new Recitals 5(a) and 5(aa) of the amended draft MiCAR).

The PoW Regime Under the New Draft MiCAR – To Be Handled With Care

As a compromise between, on the one hand, the commercial interest of opening the EU market to the best-known crypto-assets that are using PoW and, on the other hand, the preservation of the EU environmental and sustainability commitments, the revised draft MiCAR ultimately provides for:

- no specific restrictions or bans on the use of PoW in the EU crypto-assets arena;
- a highlight on the importance of limiting consensus mechanisms that could represent a threat to the environment on a small scale only, while encouraging the deployment of more environmentally friendly solutions (new Recitals 5(a) and 5(a)(a)); and
- further disclosure requirements on crypto-asset issuers, as to the inclusion in the relevant white paper of (i) “*an independent assessment of the likely energy consumption of the crypto-asset where the proof-of-work model is used*” (Article 5.1, point (bb)), and (ii) “*information on sustainability indicators related to the issuance of the crypto-asset, including whether it has been mined in compliance with the EU sustainable finance taxonomy*” (Article 5.1, point (bc)).

The above disclosure must be complied with by duly completing the applicable standard forms, formats, and templates of white papers that will be developed by ad hoc technical standards the European Securities and Markets Authority will issue separately after consultation with the European Banking Authority (Article 5(11) MiCAR).

⁷ See also the “Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee on a Digital Finance Strategy for the EU,” 24 September 2020.

Conclusion

While the ECON Committee’s approach may appear consistent with the MiCAR scope of widening and harmonising the crypto-asset market across the EU zone, environmental concerns have become a key factor in developing this new legislation. Aside from the current controversy over non-sustainability of bitcoins, operators and investors in crypto-assets must evaluate, address, and disclose the impact of their trades and services across the EU zone, with the goal of preferring and developing sustainable new technologies.

[Click here to view the latest draft MiCAR](#) (which reflects the most recent proposed changes in “track changes” format).

Authors

This GT Alert was prepared by:

- [Mariafrancesca De Leo](#) | + (39) 02.771971 | Mariafrancesca.DeLeo@gtlaw.com
- [Alessandra Boffa](#) | + (39) 02.771971 | Alessandra.Boffa@gtlaw.com
- [Bertone Biscaretti di Ruffia](#) | + (39) 02.771971 | Bertone.BiscarettidiRuffia@gtlaw.com
- [Davide Romeo](#) | + (39) 02.771971 | Davide.Romeo@gtlaw.com
- [Antonio Enrico Izzi](#) | + (39) 02.771971 | Antonio.Izzi@gtlaw.com
- [Sara Bernasconi](#) [~] | + (39) 02.771971 | Sara.Bernasconi@gtlaw.com

[~] *Not admitted to the practice of law.*

Albany. Amsterdam. Atlanta. Austin. Boston. Charlotte. Chicago. Dallas. Delaware. Denver. Fort Lauderdale. Germany. [~] Houston. Las Vegas. London. ^{*} Long Island. Los Angeles. Mexico City. ⁺ Miami. Milan. ^{*} Minneapolis. New Jersey. New York. Northern Virginia. Orange County. Orlando. Philadelphia. Phoenix. Portland. Sacramento. Salt Lake City. San Francisco. Seoul. [∞] Shanghai. Silicon Valley. Tallahassee. Tampa. Tel Aviv. [^] Tokyo. ^{*} Warsaw. ⁻ Washington, D.C.. West Palm Beach. Westchester County.

This Greenberg Traurig Alert is issued for informational purposes only and is not intended to be construed or used as general legal advice nor as a solicitation of any type. Please contact the author(s) or your Greenberg Traurig contact if you have questions regarding the currency of this information. The hiring of a lawyer is an important decision. Before you decide, ask for written information about the lawyer's legal qualifications and experience. Greenberg Traurig is a service mark and trade name of Greenberg Traurig, LLP and Greenberg Traurig, P.A. [~]Greenberg Traurig's Berlin office is operated by Greenberg Traurig Germany, an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. ^{}Operates as a separate UK registered legal entity. ⁺Greenberg Traurig's Mexico City office is operated by Greenberg Traurig, S.C., an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. [»]Greenberg Traurig's Milan office is operated by Greenberg Traurig Santa Maria, an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. [∞]Operates as Greenberg Traurig LLP Foreign Legal Consultant Office. [^]Greenberg Traurig's Tel Aviv office is a branch of Greenberg Traurig, P.A., Florida, USA. [▫]Greenberg Traurig's Tokyo Office is operated by GT Tokyo Horitsu Jimusho and Greenberg Traurig Gaikokuhojimbengoshi Jimusho, affiliates of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. [~]Greenberg Traurig's Warsaw office is operated by GREENBERG TRAUIG Nowakowska-Zimoch Wysokiński sp.k., an affiliate of Greenberg Traurig, P.A. and Greenberg Traurig, LLP. Certain partners in GREENBERG TRAUIG Nowakowska-Zimoch Wysokiński sp.k. are also shareholders in Greenberg Traurig, P.A. Images in this advertisement do not depict Greenberg Traurig attorneys, clients, staff or facilities. No aspect of this advertisement has been approved by the Supreme Court of New Jersey. ©2022 Greenberg Traurig, LLP. All rights reserved.*