

Facebook's Libra: A case for capital markets supervision?

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Received (in revised form): 6th September, 2019

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ABSTRACT

This paper considers some of the seemingly simple questions that people have been asking about

Facebook's Libra, with particular regard to its legal nature. As this paper will show, thanks to the way Libra is structured, it falls under various aspects of European capital markets law. The paper argues that the Libra Association and its resellers will most likely be required to operate properly licensed branch(es) or registered office(s) in the EU. Otherwise, they would not be allowed to market and operate their network on the EU single market. Libra is a complex product combining the functions of traditionally separate product types (namely payment instruments and funds/financial instruments). In this way, it embodies the very risks that capital market regulation seeks to control and mitigate — shrouding these risks in an innovative and exciting technical guise does not change this fact.

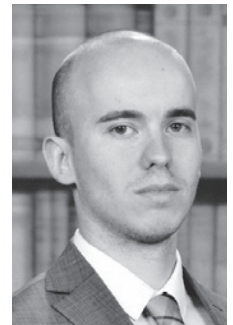
Keywords: blockchain, crypto-assets, Libra, Facebook, virtual currencies, capital markets law

INTRODUCTION

According to its white paper of June 2019,¹ it is Libra's mission to create 'A simple global currency and financial infrastructure that empowers billions of people'. The Libra coin ('Libra') aims to create a stable 'alternative currency' and an open and interoperable ecosystem of financial services. The goal of this alternative currency is to make the benefits of crypto-assets (in particular, decentralisation and fast and cheap transactions) available to the mass market while



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being globally accepted as a means of payment. To achieve this, Libra is planned to be fully backed by a 'reserve' of assets. In this way, it is envisioned that Libra will be free from the issues of instability and volatility that have plagued traditional cryptocurrencies such as Bitcoin, thereby creating a genuine store of value and a real alternative to national currencies. Libra is thus supposed to be a form of 'stable coin'.²

A phenomenon such as Libra does not exist in a legal vacuum. Despite the fact that crypto-assets do not yet pose a significant risk for financial stability,³ various supervisory authorities around the world are following its development closely.⁴ The strong interest of supervisors and the media is understandable considering the ambitious vision and immense influence of the founding members of the project. Indeed, according to the Financial Stability Board, Libra could pose a significant systemic risk were it to become a globally accepted means of payment.⁵

Along with various other senior figures, the Executive Director of the Austrian Financial Markets Authority has expressed that Libra must play by the same rules as other crypto-assets. If Libra is to be used for activities that are regulated by European capital markets law, it must be regulated and supervised.⁶ This is the fundamental principle of technology-neutral supervision: the role of the supervisory authorities is to judge each case based on the type and risks of the underlying business model, regardless of its technical implementation.⁷ For this reason, not all crypto-assets are regulated. For example, crypto-assets such as exchange tokens (used as a means of payment/exchange for services *outside* their distributed ledger (DLT) system, such as Bitcoin) and utility tokens (mainly used as a means of payment/exchange for services *inside* their DLT systems) are usually outside the regulated perimeter because they do not confer any rights or claims against the issuer (and often there is no central issuer).⁸

In light of this, one might question why especially Libra — a crypto-asset that seems at first glance to be better organised, less risky and more transparent than other crypto-assets (such as Bitcoin) — should be subject to complex regulation. Libra promises value stability (through an underlying basket of assets) as a store of value and widespread acceptance as a means of payment. While the latter goal is shared with traditional crypto-assets, the former proposition differs strongly from such crypto-assets and increases the complexity of the model, as well as its proximity to traditional financial instruments and means of payment. Another important difference to traditional crypto-assets is that users will possibly have a claim against the Libra Association and/or authorised resellers (more on that below), completely changing the economic dynamic of Libra compared with other crypto-assets. The fact that Libra seems well organised does not influence the potential risks entailed by this business model — which are the reason for regulation. This is also why traditionally very professional entities such as banks and other intermediaries are strictly supervised — not because their professionalism and organisation is in question *per se* but because of the potential risks entailed by the activities they perform and to ensure that they uphold the high standards required from them.

The goal of this paper is thus to make the reader aware of some of the points of contact that Libra has with European capital markets law — of which there are many. This analysis will not cover the Libra investment token as, at the time of writing, there is not enough publicly available information for a thorough analysis. The available documentation on which the present analysis is based is vague in some places and obviously unfinished in others. As such, it cannot possibly be complete or exhaustive. This may also explain why most supervisory authorities have not yet come forward with a detailed

legal analysis themselves. For the sake of brevity, this paper will also not cover future developments currently being considered by the Libra Foundation, such as a switch to a ‘permissionless’ mode of operations.

RELEVANT FACTS FOR A PRELIMINARY LEGAL ANALYSIS OF LIBRA

Aside from the technical details of its implementation, Libra differs from traditional cryptocurrencies⁹ like Bitcoin in three main points:¹⁰

- The Libra Association controls Libra. The Libra DLT-network is thus not fully decentralised.
- Libra is a ‘permissioned blockchain’.¹¹ At the time of writing only members of the Libra Association may run validating nodes.
- Libra is backed by a ‘currency reserve’ to provide it with intrinsic and relatively stable value. This means that its value does not solely derive from its potential use but an underlying asset or value.

The Libra Association

According to its white paper, the Libra Association (‘the association’) is an independent, not-for-profit organisation based in Geneva, Switzerland, set up ‘to coordinate and provide a framework for governance for the network and reserve’.¹² The organisation was initiated by ‘Calibra’, a subsidiary of Facebook founded specifically for this purpose. Calibra will take on a leading role in the network until launch. After launch, it is not supposed to hold a privileged position over other members of the association.

At the time of writing, the association has 28 ‘founding’ members who are entitled to run a validating node in the network (which means that they validate and execute transactions according to the consensus algorithm). These members include a number of large multinational companies from various

sectors: payment service providers (eg Mastercard, Paypal, Visa), BigTechs (eg Facebook via Calibra, eBay), telecommunications and DLT enterprises (eg crypto-exchanges such as Coinbase), venture capital firms and some other stakeholders.¹³ To become a member of the association, applicants must fulfil the criteria defined in the white paper. These criteria mainly pertain to the size, stability and reputability of the applicant.¹⁴ In addition to fulfilling said criteria, a minimum investment of one Libra investment token (equal to US\$10m) is required. Surpluses generated by the management of the Libra Reserve (see below) are distributed to the holders of the investment token. Holders also have the right to vote in the council of the association.¹⁵

The Libra Reserve

The Libra Reserve¹⁶ (‘the Reserve’) will consist of a diverse range of ‘stable’ and ‘low-risk’ assets (foreign exchange and government bonds) in ‘currencies from stable and reputable central banks’.¹⁷ Every single Libra coin will be fully backed by corresponding assets in the Reserve. These assets will be ‘held by a geographically distributed network of custodians¹⁸ with investment-grade’. Users will not interact directly with the Reserve, ie they will not directly purchase assets from or for the reserve. This task will be performed by ‘authorised resellers’. The white paper states that banks, as well as traditional and crypto-exchanges will make up the bulk of these resellers.

Users can acquire Libra via resellers in exchange for fiat money. The reseller (together with the association) will create and transfer the new Libra coins on demand to the user. Any fiat money thus received by resellers must be used immediately to purchase new corresponding assets for the reserve to ensure all Libra is fully backed by the reserve. This process is reversed if a user wants to exchange their Libra for fiat

money. In this case, the required funds are provided by the reseller by selling assets from the reserve.¹⁹ The 'repurchased' Libra coins are subsequently destroyed — 'burned'. It is assumed that users will be able to buy and sell Libra via various other channels, mostly crypto-exchanges that are not part of the association or network of resellers.²⁰ However, only the association will be able to create ('mint') and destroy ('burn') Libra coins.

The main goal of this process and the Reserve is to provide Libra with relatively stable intrinsic value. Any changes to the composition of the Reserve require a qualified majority vote of the council of the association. Such changes are only supposed to be made in response to significant changes in market conditions. Active management of the Reserve is outside the scope of the association's activities. The generation of surpluses from managing the reserve may be a positive side effect but it is not the focus of the project.

Users will not receive a return from the reserve. Revenues (eg interest, realised gains from exchange rate fluctuations) will be used to support the operating expenses of the association and to expand the network. In addition to this, holders of the Libra investment token will also receive dividends from these revenues.

According to the white paper, the association will act as a 'buyer of last resort' for resellers. This means that resellers will always be able to sell Libra to the Reserve 'at a price equal to the value of the basket'.²¹ The available documentation on Libra does not state whether or not users have such a right to sell Libra back to resellers or the association as well. An intrinsic value of Libra based on the assets in the Reserve however is hardly conceivable without such a right or claim. Otherwise, from a user perspective, as is the case with Bitcoin, for example, Libra's value could only be based on its potential use and trust in the network without a

legally binding connection to the value of the reserve. Without such a connection, however, Libra would not have an intrinsic value and thus not be much different from traditional cryptocurrencies. Yet, this scenario would run diametrically opposed to the explicit intention described in the white paper. In this regard, it should also be noted that it is not clear whether the explicit legal entitlement of the user is required to establish the legal right of the user to sell Libra back to resellers. Depending on national civil law, the factual possibility of selling Libra to resellers in connection with the intent stated in the public utterances of the association (eg white papers) may be sufficient to establish the implicit right of users to sell Libra back to resellers. The present analysis thus covers both scenarios, as Libra is unlikely to succeed without conferring a claim against the issuer or network to its users.

It should also be noted that Libra will not directly represent or tokenise the assets in the Reserve. This means that users do not hold claim to these assets directly. According to the mechanism described above, however, Libra's value will, at least indirectly, be based on the value of the reserve. The value of the reserve may fluctuate. Therefore, the value of Libra will necessarily fluctuate as well, even if its goal is stability of value.²²

POTENTIALLY RELEVANT CAPITAL MARKETS LAW

Summing up the above the following relevant facts can be established regarding Libra:

- Fiat money is raised from users by resellers in exchange for Libra coins.
- The customer segment targeted by Libra will most likely include retail investors,²³ as defined by the Markets in Financial Instruments Directive as amended (MiFID II).

- It is as yet unclear whether users will be legally entitled to sell Libra to resellers and/or the association.
- Resellers are entitled to sell Libra to the Reserve.
- No further users' rights can be deduced from the available documentation.
- Libra's value relies on the value of the reserve. Each Libra coin will be 100 per cent backed by assets in the reserve. Libra does not directly represent/tokenise these assets.
- The Libra Association determines the composition of the Reserve by qualified majority.
- Transactions with users are handled by the resellers.

On this basis, the paper will elaborate on some of the potentially relevant capital markets regulation in the EU. This analysis is neither exhaustive nor final. The goal is to provide a basis for further discussions on the legal nature of Libra.

As a starting point, it should be noted the Libra Association is incorporated in Switzerland. Switzerland is not an EU member state. Therefore, the EU capital markets law will only be applicable if and when Libra conducts relevant business activities within the EU. Relevant to this, a governing principle of European capital markets law is that only undertakings situated within the EU may perform regulated activities within the EU. This means that the association and/or resellers would be required to operate a branch or registered office in the EU. Depending on which regulatory regime(s) is/are applicable to Libra, these entities would also potentially require a licence from the national competent authority of the EU member state of their residence.

Consequently, this competent authority would primarily be responsible for the supervision of activities in connection with Libra. Where business is conducted in a member state other than the state of residence, the

competent authorities of both states would have to cooperate in the supervision of these activities. As Libra is set out to establish a global presence, the European Supervisory Authorities as well as the national competent authorities of all 28 member states could potentially be involved, creating further complexity.

It should also be noted that even if Libra were not marketed in the EU, users could still get access to Libra through off-shore services in non-member states. In such cases, difficult legal questions arise as the definition of 'distribution' varies between supervisory regimes. Libra plans to integrate its payment services with platforms and other services provided to retail clients. If these services are marketed in the EU, the definition of distribution within the EU would most likely be fulfilled in many cases. To illustrate this, one might think of an EU-based online shopping website that accepts payment in Libra and provides weblinks to authorised Libra resellers or wallet service providers. Ultimately, however, the issue is largely academic as the Libra Foundation has expressed its intention to offer Libra worldwide with no restrictions foreseeable in the important EU market. Additionally, the Libra Foundation has also stated that it does not intend to circumvent existing capital markets law and is willing to cooperate with regulators.

Is Libra a payment instrument or payment service under PSD2? Is Libra e-money under the E-Money Directive?

Libra aspires to be an alternative to traditional currencies issued by nation states. It is therefore not too far-fetched that it could potentially be qualified as a payment instrument according to Art 4(14) PSD2.²⁴ Such instruments are described as 'a personalised device(s) and/or set of procedures agreed between the payment service user and the payment service provider and used

in order to initiate a payment order' (Art 4(14) PSD2). This is a rather broad legal term. Any instrument that can be used to initiate a payment order (Art 4(13) PSD2) is covered — provided that it is personalised. 'Personalisation' in this regard means that it cannot be used by any bearer, ie not anyone in possession of it, and is thus not transferable (eg a credit card).²⁵ This does not seem to be the case with Libra — the white paper does not present any kind of personalisation of the Libra coin. Anyone who holds Libra can use it, regardless of whom it was issued to. Libra should therefore not be considered a payment instrument under PSD2.

At first glance, it also seems plausible that Libra could be electronic money according to Art 2(2) E-Money Directive ('EMD')²⁶. As defined in point 5 of Article 4 of Directive 2007/64/EC,²⁷ 'electronic money' refers to monetary value stored electronically, including magnetically, as represented by a claim on the issuer which is issued on receipt of funds for the purpose of making payment transactions and which is accepted by a natural or legal person other than the electronic money issuer.

For Libra to be considered electronic money, it would have to represent a claim of the user on the issuer, ie the resellers and the association respectively. As stated above, it is unclear whether Libra will convey such a claim to its users. Should such a claim not exist, Libra cannot by definition be electronic money. If, however, one can accept the idea, that Libra may (have to) convey said claim against the issuer, it is possible that national competent authorities may come to the conclusion that it is indeed electronic money, as the obvious intention is to use it to conduct payment transactions within the wide meaning of point 5 of Article 4 PSD2. According to Art 10 EMD, only electronic money issuers in the sense of Art 1(1) *leg cit* may issue electronic money. For Libra this means that the foundation or the resellers (it is unclear who effectively 'mints' new Libra

coins) would have to acquire a licence, as either an EU (CRR) credit institution or an electronic money institution according to Art 2(1) *leg cit*. It should also be noted that Art 3(5) of the EMD prohibits electronic money institutions from issuing electronic money through agents. This prohibition may be relevant regarding the activities of resellers. Further, it should be considered that according to Art 11(2) EMD, the electronic money issuer has to redeem electronic money at any moment and at par value the monetary value of the electronic money held. This may be problematic as Libra's value will not be stable to any single currency, thus pointing to the conclusion that Libra may in fact not be electronic money as it does not represent one specific currency.

If one comes to the conclusion that Libra is neither electronic money nor a payment instrument according to PSD2, it may still potentially fall under the wider definition of Annex I no. 5 of the Capital Requirements Directive (CRD) IV²⁸ and may thus constitute a regulated activity reserved for licensed credit institutions in many jurisdictions. Annex I no. 5 reads 'Issuing and administering other means of payment (eg travellers' cheques and bankers' drafts) insofar as such activity is not a payment service according to Art 4(3) in connection with Annex I Directive 2007/64/EC, in which case it would constitute a regulated activity under the PSD. Regarding this wide definition, the Austrian Supreme Administrative Court has ruled that the provision transposing it into the Austrian Bankwesengesetz encompasses 'all generally accepted money surrogates, which are accepted by a comparatively large group of persons as a means of payment'.²⁹

According to its own white paper, Libra is intended as a simple global currency and financial infrastructure that empowers billions of people.³⁰ Should it get remotely close to this goal, it would presumably constitute the kind of generally accepted money

surrogate described in Annex I no. 5 CRD IV. Thus, the central issuance and administration of Libra within the European Union by the association and resellers may very well constitute a regulated activity that requires a bank licence under CRD IV.

Fund-like structure

Aside from the payment-centric considerations outlined above, the fund-like structure of Libra is particularly striking considering the design and composition of the reserve. Users can purchase Libra with fiat money. As a direct consequence of the purchase new assets for the Libra Reserve, which is managed by the Libra Association, are purchased. Investors seem thus to be able to exchange Libra directly against fiat money via the resellers to the detriment of the fund's assets. Given that the number of Libra coins is also generally not limited, Libra could constitute an open-end fund.

Following this train of thought, the classification of Libra as an undertaking for collective investment in securities (UCITS) within the meaning of the UCITS framework is conceivable.³¹ The qualification as a UCITS requires that the units of an undertaking are — at the request of holders — repurchased or redeemed, directly or indirectly, out of the undertakings' assets. As stated above, it is unclear whether Libra will convey such a (direct) claim to its users. However actions taken by a UCITS to ensure that the stock exchange value of its units does not significantly vary from their net asset value could be regarded as equivalent to such repurchase or redemption.³² Such measures can be assumed due to the fact that Libra's value relies directly and exclusively on the value of the reserve. It should however be noted that whether a collective investment undertaking should be considered a UCITS without granting a repurchase or redemption claim to its investor is a contentious issue.³³

Even assuming that Libra conveys such a claim or undertakes stabilising actions, as described above — depending on the national law transposing the Directive 2009/65/EC ('UCITS Directive'), other national provisions may prevent the UCITS Directive from being applicable. In Austria for example, the Libra Fund cannot by definition constitute a UCITS without being approved in accordance with Article 50 of the Austrian Investment Fund Act 2011 or in its home member state in accordance with Article 5 of the UCITS Directive. Furthermore, it should be considered that the UCITS framework is regarded as a 'gold standard', both inside and outside the EU. This status is due in particular to its clear and stringent rules. It seems questionable to which extent Facebook or the Libra Association aim to fulfil those high requirements and standards in order to attain such a 'gold standard'.

Therefore, it is more likely that Libra could fall under the scope of the Alternative Investment Fund Managers Directive (AIFMD).³⁴ Pursuant to Article 4 AIFMD, any collective investment undertaking, including investment compartments thereof, which raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors and do not require authorisation pursuant to Article 5 of UCITS Directive constitutes an alternative investment fund (AIF). These criteria must be interpreted in light of the ESMA Guidelines on the key terms of the Directive on Alternative Investment Fund Managers. According to the guidelines, an undertaking pursuing a general commercial or industrial purpose should not be considered an AIF.³⁵ In this regard, ESMA also states that competent authorities and market participants should not consider that the absence of all or any one of the characteristics as exemplarily set out in the guidelines, conclusively demonstrates that an undertaking does not fulfil the relevant characteristic.

Competent authorities and market participants should consider an undertaking to be an AIF if the presence of all the concepts in the definition under Article 4(1)(a) of the AIFMD is otherwise established.³⁶ Thus, it is also necessary to take into account the economic aspects of the undertaking.³⁷

The 'Libra Fund' would appear to meet all the criteria of an AIF, therefore making it subject to the AIFMD regime: Capital is raised by raising fiat money from an indefinite number of investors in order to invest it into various short-term assets, thereby at the very least creating a 'value preserving reservoirs of liquidity' — and thus a benefit for the investors — without any other general commercial or industrial purpose, which predominantly determines the business activity and to which the capital is therefore contributed. From an economic point of view, Libra also has obvious similarities to a money market fund: the capital raised is invested in low-risk short-term assets, in particular for the purpose of value preservation.

Member states may allow non-EU AIFMs to market to professional investors, in their territory only, units or shares of AIFs they manage, as far as they fulfil the conditions laid down in Article 42 AIFMD. However, member states may also impose stricter rules on the non-EU AIFM in respect of the marketing of units or shares of AIFs to investors in their territory. For example, if a non-EU AIFM proposes to market units or shares of an AIF in Austria, it must file to the Austrian Financial Markets Authority a notification letter for each AIF it proposes to market. Additionally, various other documents and information must be provided, such as a declaration by the non-EU AIFM that it undertakes to comply with the requirements stipulated in the Austrian Alternative Investment Fund Managers Act 2013, in the AIFMD, and in the delegated acts adopted on the basis of the AIFMD for the entire duration that the AIF is marketed in Austria.

The Austrian Financial Markets Authority must forbid further marketing of AIFs if the notification has not been lodged, or the non-EU AIFM breaches the obligations arising from the aforementioned declaration. Even if the marketing of the Libra Fund is allowed under the conditions mentioned above, another fundamental consequence must be pointed out. Depending on the national transposition of the AIFMD,³⁸ the marketing of units and shares of the Libra Fund to retail investors could be *ex lege* prohibited, eg as it is the case in Austria. Therefore, taking into account all the considerations above, the Libra Association may have to consider whether it would not be more beneficial to comply with the provisions of the UCITS regime. This would include setting up a legal entity in the European Union that manages the Libra UCITS fund.³⁹

Finally, it should be noted that Libra's investment strategy is similar to that of a money market fund. The classification as a money market fund within the meaning of the Money Market Funds Regulation (MMFR),⁴⁰ which has been in force since 21st July, 2018, is therefore a realistic possibility. The regulation applies to both UCITS and AIFs that invest in short-term assets and have distinct or cumulative objectives offering returns in line with money market rates or preserving the value of the investment. In this case, the comprehensive provisions of the MMFR must be observed. In addition to extensive reporting and stress-test obligations, stricter liquidity requirements as well as rules on portfolio diversification would also apply on top of the UCITS or AIFMD regime.

Libra might also constitute the taking of a deposit (CRD IV) or a transferrable security (MiFID II, prospectus regulation)

Due to its structure and mainly the fact that Libra is exchanged for money from the

public, a number of other regulatory regimes may also be applicable. Foremost among them are ‘taking deposits and other repayable funds’ according to Annex I no. 1 CRD IV as well as the regimes of MiFID II and the prospectus regulation⁴¹ as Libra potentially constitutes transferrable securities according to Art 4 (1) point (44) MiFID II⁴² and thus a financial instrument in line with Annex I section C point (1) MiFID II. Additionally, units in an AIF are also financial instruments under MiFID II.⁴³

Both deposits⁴⁴ and transferable securities⁴⁵ require some kind of claim to (re-) payment against the party receiving the funds or the issuer. As already discussed, it is currently uncertain whether such a claim exists. Assuming it does not exist none of the provisions above would be applicable.⁴⁶

If on the other hand, a claim against the association and/or the resellers is assumed, both regimes may very well be applicable. In reality, such a claim would not necessarily amount to 100 per cent of the funds paid in by the user, as Libra’s value may fluctuate relative to the currency used for the purchase of Libra. This does not however mean that Libra does not constitute the taking of a deposit as, for example, the payout for structured deposits also fluctuates. Another illustration of this concept is that in Austria, for example, it is accepted that deposits according to Art 1 (1) no. 1 case 1 Austrian BWG do not require repayment of the full amount deposited.⁴⁷ In this case, the exchange of Libra for fiat money would constitute a regulated activity according to the CRD IV and require the according licence.

From a MiFID II and prospectus-perspective, Libra can be considered as a structured bond based on a basket of currencies and debt instruments, ie the Reserve. Following this line of thinking, it is also not unreasonable to assume that Libra may fall under the Benchmark-Regulation,⁴⁸ as calculating and providing data on the value of the reserve may fall within the

definition of Art 3(1) point (5) Benchmark-Regulation. The last criterion required for a transferrable security — transferability or tradability⁴⁹ — seems unproblematic considering Libra is designed as a crypto-asset and the white paper mentions no restrictions in this regard.

The consequences of this classification are far-reaching. The provision of investment services in connection with the Libra coin (most importantly the reception and transmission of orders in relation to Libra⁵⁰ but also the operation of trading facilities, ie multilateral or organised trading facilities⁵¹) would require either a bank licence according to CRD IV or a licence as an investment firm according to MiFID II. The same is true for safekeeping and administration of Libra as a security.⁵² In addition to this, a public offer of Libra to retail investors would require the publication of a prospectus in compliance with the Prospectus-Directive⁵³ as it would constitute an ‘offer of securities to the public’ according to Art 2 lit (d) Prospectus-Directive. Were Libra classified as an AIF, however, this would not apply as units in AIF are exempt from the Prospectus-Directive per Article 1(2) lit (a).

PRIIPs

Like the definition of transferable securities and deposits, the applicability of the packaged retail investment and insurance-based product (PRIIP) regulation⁵⁴ hinges on a claim to an amount repayable against the manufacturer of the product. Art 4(1) PRIIP-Regulation defines which products fall within the scope of the regulation:

“‘packaged retail investment product’ or ‘PRIIP’ means an investment ... where, regardless of the legal form of the investment, the amount repayable to the retail investor is subject to fluctuations because of exposure to reference values or to the

performance of one or more assets which are not directly purchased by the retail investor’.

According to the available documentation, Libra will be offered to retail investors and its value will fluctuate based on the value of the reserve. The assets in the reserve are also not directly acquired by the retail investors. Recital (6) of the PRIIP-Regulation explicitly states that the regulation applies to all products, regardless of their form or construction. Consequently, a product does not necessarily have to be a financial instrument under MiFID II to qualify as a PRIIP. Where Libra conveys a claim to an amount repayable to the investor, Libra falls within the core of the definition of a PRIIP. This shows that based on their individual design, crypto-assets can (and in some cases arguably already do) fall under the PRIIP-Regulation — a fact that has so far mostly been overlooked in the related discourse. It is however perfectly in line with the principle of technology-neutral supervision.⁵⁵

The PRIIP-Regulation obliges manufacturers of PRIIPs to draw up and publish on their website a key information document on the product of three pages, the PRIIP-KID.⁵⁶ Persons selling a PRIIP are obliged to provide retail clients with the PRIIP-KID in good time before the retail investor is bound by any contract or offering relating to the PRIIP.⁵⁷ For both manufacturer and distributor, selling or offering a PRIIP without a PRIIP-KID is strictly prohibited.

Anti-Money-Laundering-Directive (AML)

Regardless of the considerations above and whether a claim to repayment exists or not, Libra is likely to qualify as a ‘virtual currency’ in accordance with Article 3(18) of the 5th Anti-Money-Laundering Directive (5AML).⁵⁸ Thus, all actors that provide

services to safeguard private keys (‘wallets’) or are engaged in exchange services between Libra coins and fiat currencies would be regarded as ‘providers engaged in exchange services between virtual currencies and fiat currencies’ according to Article 2(1) point 3 lit (g) and custodian wallet providers (lit (h)) of 5AML. Furthermore, one must keep in mind the FATF Standards, which have recently been updated and are usually expected to be complied with by EU member states. In addition to the activities mentioned above, all entities that provide the transfer⁵⁹ of virtual assets and the participation in and provision of financial services related to an issuer’s offer and/or sale of a virtual asset are regarded as virtual asset services providers under the FATF Standards.

This would affect both Calibra, which intends to offer a Libra coin wallet, as well as any resellers and crypto exchanges involved. If they provide or market their services in the EU, they are subject to the various national laws transposing 5AML, especially with regard to due diligence and reporting obligations. In accordance with Article 47(1) 5AML, they must also be licensed or registered prior to the provision of such services.

CONCLUSION

The question that inspired this paper: ‘Is Libra a case for capital markets supervision?’ must be answered with a resounding ‘yes’. Due to the global nature of the project, it seems almost certain that Libra will be active in the EU single market. By doing so, it will be subject to European capital markets law (or its respective transposition into the national laws of the member states). This means that should any of the regulatory regimes described above be applicable, the Libra Association and/or its authorised resellers will be required to establish a legal presence in EU territory. Should the

Libra Association not establish such a presence in every single member state or the various resellers conduct their business across borders, Libra will require international supervision from both the national competent authorities of the member states involved and the European Supervisory Authorities (mainly ESMA and EBA).

The multitude of capital markets regimes potentially applicable to Libra once again shows how complex and multifaceted the phenomenon of crypto-assets is. Depending on its actual implementation, Libra could be e-money, a means of payment or deposit according to CRD IV, a UCITS or an alternative investment fund and/or a structured bond under MiFID II. Each of these regimes imposes a wide range of regulatory duties on the Libra Association and its resellers. Furthermore, it is very likely that the information requirements *vis-à-vis* retail clients laid down in the PRIIP-Regulation as well as the strict 5AMLD regime are applicable to Libra's operations. Assuming that Libra does not convey a right to payback or redemption to users, it seems that the classification of Libra as an alternative investment fund and the application of 5AMLD remain as the most probable result of future legal analysis by supervisory authorities. As offering Libra, as an AIF, to retail investors would be severely restricted within the EU, it would be highly advisable for the Libra Association to consider setting up Libra as a UCITS instead.

Crypto-assets do not exist in a legal vacuum. Regardless of society's enthusiasm for new technologies or disillusionment with the traditional financial sector, it is essential to keep one fundamental truth in mind: whatever technical guise an otherwise strictly regulated business model is shrouded in, one cannot disregard the protection offered to consumers by the European single market, no matter how exciting the technology might be or how powerful and influential the actors behind the business model are.

AUTHORS' NOTE

This paper reflects the personal legal opinion of the authors. It is not an official position of the Austrian Financial Markets Authority.

REFERENCES AND NOTES

- (1) Libra Association (2019) 'Libra white paper — Introduction', available at: <https://libra.org/en-US/white-paper/#introduction> (accessed 5th September, 2019).
- (2) A stable coin is a type of crypto-asset that derives intrinsic value from a currency or other underlying asset such as gold. Stable coins are thus not (at least in theory) subject to volatility and price speculation like, for example, Bitcoin. Libra, however, is based on the value of a basket of different underlyings. Without judging the merit of this approach, it has to be stated that this means that Libra will not be stable relative to any single currency. In addition to this, the Libra Association has the power to change the composition of the reserve. We therefore come to the conclusion that Libra is not a stable coin in the classic sense of the term. See also: Bofinger, P. (2019) 'Libra: Facebook's new currency fails the Hayek test', available at: <https://www.socialeurope.eu/libra-facebooks-new-currency> (accessed 5th September, 2019).
- (3) Financial Stability Board (2019) 'Crypto-asset markets — Potential channels for future financial stability implications', available at: <https://www.fsb.org/wp-content/uploads/P101018.pdf> (accessed 5th September, 2019).
- (4) Stacey, K. and Binham, C. (2019) 'Global regulators deal blow to Facebook's Libra currency plan', *Financial Times*, 25th July, available at: <https://www.ft.com/content/0c1f3832-96b1-11e9-9573-ee5cbb98ed36> (accessed 5th September, 2019).
- (5) Financial Stability Board (2019) 'Crypto-assets — Work underway, regulatory approaches and potential gaps', available at: <https://www.fsb.org/wp-content/uploads/P310519.pdf> (accessed 5th September, 2019).
- (6) DiePresse (2019) 'FMA will Facebook-Währung "Libra" regulieren', available at: <https://diepresse.com/home/wirtschaft/boerse/5650246/FMA-will-FacebookWaehrung-Libra-regulieren> (accessed 5th September, 2019).
- (7) Austrian Financial Markets Authority (2018) 'Financial Technology — FinTech', available at: <https://www.fma.gv.at/fina-aktuell/financial-technology-fintech/> (accessed 5th September, 2019).
- (8) See also Financial Conduct Authority (2019) 'Guidance on Cryptoassets Feedback and Final Guidance to CP 19/3, PS19/22', available at: <https://www.fca.org.uk/publication/policy/ps19-22.pdf> (accessed 5th September, 2019).
- (9) Further information on the legal nature of crypto-assets can be found in Rirsch, R. and Tomanek, S.

- (2018) 'Crypto-assets: Commodities under European financial markets law?' *Journal of Financial Compliance*, Vol. 2 No. 3, pp. 199–206.
- (10) Libra Association, ref. 1 above.
- (11) The designation 'blockchain' may have been chosen more for marketing reasons than based on the actual technical setup of the network. From a technical point of view, Libra gathers transactions into blocks for verification in the execution-phase. It does however not store them on the DLT in this form — instead, every single transaction is hashed and stored separately. For more detailed information, see: Libra Association (2019) 'The Libra Blockchain', available at: <https://developers.libra.org/docs/assets/papers/the-libra-blockchain.pdf> (accessed 5th September, 2019).
- (12) Libra Association, ref. 1 above.
- (13) Libra Association (2019) 'How to Become a Founding Member — Overview', available at: <https://libra.org/en-US/becoming-founding-member/?noredirect=1#overview> (accessed 5th September, 2019).
- (14) Libra Association (2019) 'How to Become a Founding Member — Member Evaluation Criteria', available at: <https://libra.org/en-US/becoming-founding-member/?noredirect=1#overview> (accessed 5th September, 2019).
- (15) Libra Association (2019) 'The Libra Association — 2: Libra Association Council', available at: https://libra.org/en-US/association-council-principles/?noredirect=1#libra_association_council (accessed 5th September, 2019).
- (16) Libra Association (2019) 'The Libra Reserve', available at: https://libra.org/en-US/about-currency-reserve/?noredirect=1#the_reserve (accessed 5th September, 2019).
- (17) It is assumed these will include among others the US dollar, GBP pound, Swiss franc and Japanese yen, as well as liquid short-term (government) debt instruments issued in these currencies. See also Constine, J. (2019) 'Facebook announces Libra cryptocurrency: All you need to know, The Libra currency — a stablecoin', available at: <https://techcrunch.com/2019/06/18/facebook-libra/> (accessed 5th September, 2019).
- (18) The safekeeping and administration of securities is defined in Annex I No. 12 of Directive 2013/36/EU and regulated to varying degrees in the member states of the EU. In some it requires a banking licence, such as in Austria, according to Art 1 (1) of the Austrian Depotgesetz.
- (19) In both cases, the present study assumes that the process of buying and selling assets for the reserve is not conducted on a per user transaction basis but in bulk, which may lead to a slight time lag and correspondingly expose the reseller and/or foundation to the short-term risk of fluctuating prices.
- (20) Even if the association wanted to prohibit such activities, it will be difficult to stop such activities unless technical restrictions on the transferability of Libra are put in place. Such restrictions, however, will not be able to solve the issue of off-chain transactions — ie the offline transfer of wallets/keys between users.
- (21) Libra Association (2019) 'Libra white paper — 05 The Libra Association', available at: <https://libra.org/en-US/white-paper/#the-libra-currency-and-reserve> (accessed 5th September, 2019). See also ref. 2 — we hold that Libra will never be stable in relation to a single currency.
- (22) Libra Association (2019) 'Libra white paper — 04 The Libra Currency and Reserve', available at: <https://libra.org/en-US/white-paper/#the-libra-blockchain> (accessed 5th September, 2019).
- (23) Art 4(11) in conjunction with Annex II MiFID II.
- (24) Directive (EU) 2015/2366.
- (25) See also the FinTech-Navigator provided by the Austrian Financial Market Authority: 'Welche Coins bzw Token fallen unter das Zahlungsdienstegesetz 2018', available at: <https://www.fma.gv.at/querschnittsthemen/fintechnavigator/initial-coin-offering/> (accessed 5th September, 2019).
- (26) Directive 2009/110/EC.
- (27) Directive 2007/64/EC is the predecessor directive to PSD2. Art 4 point 5 PSD is identical to Art 4 point 5 PSD2 aside from the fact that the PSD2 definition also covers act initiated on behalf of the payer: 'payment transaction' means an act, initiated by the payer or on his behalf or by the payee, of placing, transferring or withdrawing funds, irrespective of any underlying obligations between the payer and the payee'.
- (28) Directive 2013/36/EU.
- (29) Austrian Supreme Administrative Court, 7th February, 2017, W158 2124948-1.
- (30) Libra Association, ref. 1 above.
- (31) See Recital (5) and Article 3 lit a) Directive 2009/65/EC.
- (32) See Article 1(2) lit b) Directive 2009/65/EC.
- (33) See eg Leixner, I. in Bollenberger/Kellner, Investmentfondsgesetz (2016), § 2 no 12.
- (34) Directive 2011/61/EU of the European Parliament and of the Council of 8th June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.
- (35) European Securities and Markets Authority (2013) 'Final report on the Guidelines on key concepts of the AIFMD of 24 May 2013' (ESMA/2013/600), IV.12.
- (36) European Securities and Markets Authority, ref. 35 above, III. 5.
- (37) See also Hellwagner, R. /Seeber, T, AIFMG und Stiftungen, ÖBA 2018, p.23 ff.
- (38) See Article 43 of Directive 2011/61/EU.
- (39) For example, in Austria, the government strongly promotes and supports digital innovation and the creation of a digitally-friendly environment; see: Federal Ministry Republic of Austria Digital and Economic Affairs (2018) 'Future Strategy', available at: <https://www.en.bmdw.gv.at/Digitalisation/>

- Future_strategy/Seiten/default.aspx (accessed 5th September, 2019).https://www.en.bmdw.gv.at/Digitalisation/Future_strategy/Seiten/default.aspx
- (40) Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds.
- (41) Regulation (EU) 2017/1129.
- (42) Which Art 2 lit (a) of the prospectus regulation refers to.
- (43) Annex I section c point (3) MiFID II.
- (44) See also: Waldherr, M., Ressnik, K. and Schneckleitner, T. (2017) in Dellinger, M. (ed.), 'Bankwesengesetz — Kommentar', § 1–Z 1, Einlagengeschäft, p. 17, No. 19 f, LexisNexis, Vienna.
- (45) See also: Kalss, S., Oppitz, M. and Zollner, J. (2015) 'Kapitalmarktrecht', § 11–B, Angebotsgegenstand, p. 387 No. 15, Linde Verlag, Vienna; Zivny, T. (2016) 'KMG', § 1–D, Wertpapiere (§1 Abs 1 Z 4) – 1, Allgemein, No. 69, MANZ Verlag Wien, Vienna.
- (46) The Austrian Financial Market Authority also names such a claim as a requirement for crypto-assets to be considered transferrable securities, see: FMA (2018) 'FinTech Navigator, Wann liegt ein Wertpapier iSd KMG/WAG 2018 vor?', available at: <https://www.fma.gv.at/querschnittsthemen/fintechnavigator/initial-coin-offering/> (accessed 5th September, 2019).
- (47) Raschauer, B. (2015) 'Finanzmarktaufsichtsrecht', C. Bankgeschäfte gemäß § 1 BWG, p.118 f, Verlag Österreich, Vienna.
- (48) Regulation (EU) 2016/1011.
- (49) FMA (2018) 'Aufsichtsrechtliche Einordnung von Coins und Tokens, Wann liegt ein Wertpapier iSd KMG/WAG 2018 vor?', available at: <https://www.fma.gv.at/querschnittsthemen/fintechnavigator/initial-coin-offering/> (accessed 5th September, 2019).
- (50) Annex I section A point (1).
- (51) Annex I section A points (8) and (9).
- (52) Annex I No. 12 of Directive 2013/36/EU.
- (53) Art 3(1) Prospectus-Directive.
- (54) Regulation (EU) No 1286/2014.
- (55) It should be noted that most 'traditional' cryptocurrencies do not convey a claim against the issuer. Therefore they do not fall within the scope of the PRIIP-Regulation.
- (56) Art 5(1) PRIIP-Regulation.
- (57) Art 13 PRIIP-Regulation.
- (58) Directive (EU) 2018/843.
- (59) 'In this context of virtual assets, transfer means to conduct a transaction on behalf of another natural or legal person that moves a virtual asset from one virtual asset address or account to another'; see Financial Action Task Force on Money Laundering (2019) 'International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation — The FATF Recommendations (Updated June 2019)', available at: <http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf>, p. 127 (accessed 5th September, 2019).