The EU view onblockchain

Blockchain technology has grown in both reputation and popularity at a time where the UK is at a tipping point and could be overthrown by a potential Brexit. The European Union has been brought to the forefront of all discussions and examined under a magnifying glass by both Brexiters and Bremainers. This heated political debate has been overshadowing some of the main European Union's decisions.

What exactly is the EU planning to do in terms of regulating blockchain?

In the hope of untangling truths from lies, EPI met with Monica Monaco, the founder and president of TrustEuAffairs, a company that advises its clients on EU legislative relevant initiatives. Having worked for ten years as a senior manager of regulatory affairs for Visa Europe in Brussels before funding TrustEuAffairs in 2013, Monaco offers an important insight in the regulatory framework of the European Union.

Blockchain at the European Level

Monaco explains to EPI that although blockchain is being discussed and debated by the European institutions, this is mainly in the context of virtual currencies. Currently, the European Union is not planning to regulate this new technology, but is trying to understand its potential uses. There is for example a starting reflection in the European Commission Directorate General CONNECT about the social uses of the blockchain, including tracing provenance in the food supply chain. Rather than focusing on regulation this reflection seems to focus on possible standardisations needs, and it is at a very early stage, since the first meeting about this strand of work took place on the 21st of June 2016.

A report from the European Parliament under the name "Virtual Currencies" , written by the German MEP Weiszacker, resulted in the adoption of a resolution by the European Parliament on the 26th of May. The resolution highlights the opportunities and risks that VCs and DLT pose in the technological landscape of payments, and states that VCs and DLT have the potential to contribute positively to citizens' welfare and economic development, including in the financial sector, by lowering transaction and operational costs for payments and especially cross-border transfer of funds, and reducing the cost of access to finance, potentially contributing to financial inclusion. However, according to the resolution, VC and DLT schemes entail risks due to the absence of a governance structures ,the high volatility of VC and the absence of traditional forms of regulatory supervision, safeguards and protection, issues which are especially challenging for consumers. The resolution proposes the development of a sound legal framework that keeps up with innovation, ensuring a timely and proportionate response if and when the use of some distributed ledger technology applications becomes systemically relevant.

Monaco said: “The report is what they call an “INI” which is an own initiative report: the report was prepared by the Economic Committee on its initiative due to the interests of the members of the Committee in the matter and not as happens for the majority of the reports to respond to a draft legislative proposal coming from the European Commission. This means we are a very early stage in terms of possible regulation ”.

Conflicting views on blockchain

The aforementioned report portrays blockchain technology in a somewhat positive light, describing it as a new technology that can help organise data and relate that data to other types of data. The communiqué suggests that it is interesting to investigate the possible uses of blockchain technology: it can not only be applied to money transfers but also to smart contracts, land registers and different types of inventories. According to Monaco, blockchain is a new tool which can allow for the provision of comprehensive, rich information and for automated verification and reconciliation, and can be described as potentially carrying benefits for both businesses and users.

However, out of the 128 amendments on the European Parliament Report published on the 13th of March and voted on the 26th of April, several convey the worries of several MEPs regarding the question of the transparency behind blockchain technology.

Monaco described to EPI the division between the blockchain enthusiasts and blockchain sceptics in the European Parliament. On one side, the enthusiasts see blockchain as an opportunity due to its multiple uses that are beneficial to businesses and consumers alike, whilst the sceptics believe that you should tread carefully when it comes to blockchain.

The resolution calls for the creation of a **horizontal Task Force on distributed ledger technology** led by the Commission, consisting of technical and regulatory experts, which shall analyse the benefits and risks of distributed ledger technology and develop stress tests for all relevant aspects of virtual currencies and other distributed ledger technology schemes that reach a level of use that would make them systemically important for stability. Also, the Report asks to the Commission to develop, in cooperation with the Member States and the virtual currencies industry, **guidelines with the aim of guaranteeing that correct, clear and complete information** is provided for existing and future virtual currency users.

The issue with transparency

Monaco discloses that the critiques surrounding the transparency of blockchain is centred on the fact that “dark” versions of the main blockchain, which may not be able to be decrypted, could allow for the possibility of blurring the movement of money. The novelty of a decentralised system of payments might also be seen as a problem to regulators, especially in terms of supervision. Monaco does stress however that the blockchain, in terms of customer authentication procedures , seems to fullfill the security requirements set in the PSD2.

The counter argument presented is that blockchain might actually be too transparent and that an extensive data protection is therefore needed for the users.

“This reminds me Article 79 of the PSD1, which stated that the processing of personal data by payment systems and payment service providers should be permitted when this is necessary to safeguard the prevention, investigation and detection of payment fraud.,” said Monaco.

Educating regulators and avoiding over-regulation as a potential solution

The main obstacle that needs to be addressed, according to Monaco, is the lack of technical expertise from the regulators surrounding this new technology. She believes it is fundamental to better educate the European Institutions on virtual currencies functioning and the uses of blockchain technology.

These institutions are at the stage of discovery, a similar stage that financial services industry encountered with virtual currencies back in 2013. Monaco told EPI that if regulators are made aware of the different uses of the DLT technology and of VC , it is likely they will forge their own ideas and make sensible choices.

Monaco also praised the benefits of this new technology and believes that too much regulation could stifle the innovation in its course.

“Starting to regulate before the full development of the product doesn’t allow the sector to fully develop and, consequentially, could destroy its full potentiality,” Monaco said.

However, Monaco believes that regulation should not be completely ignored but rather turned towards anti-money laundering solutions. She predicts that the Commission may publish a law proposal that will cover anti-money laundering aspects of VC exchange platforms early July..