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Publication date

2023

Document Version

Final published version

[Link to publication](#)

Citation for published version (APA):

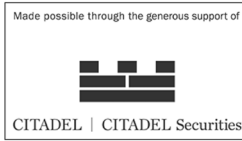
Martino, E. D. (2023). Crypto Regulation from a Comparative Perspective: A Functional Framework for the Analysis. Web publication or website, Oxford Business Law Blog. <https://blogs.law.ox.ac.uk/oblb/blog-post/2023/09/crypto-regulation-comparative-perspective-functional-framework-analysis>

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Crypto Regulation from a Comparative Perspective: A Functional Framework for the Analysis

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Posted **20 September 2023**

Time to read **3 Minutes**

OBLB categories [Financial Regulation](#)

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OBLB keywords [Cryptocurrencies](#), [Stablecoin](#), [Comparative law](#), [Cryptoassets](#), [Financial services](#)

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The financial applications of blockchain technology are gaining increasing attention in the regulatory sphere both for their growing relevance and for the several scandals and failures of the past months. The regulatory landscape is quickly and non-linearly evolving, resulting in the impossibility to capture a nitid snapshot of the international regulatory regime from a comparative perspective.



In a recent paper, forthcoming in the Research Handbook of Comparative Financial Regulation, I propose an analytical framework for a comparative approach to crypto-assets regulation. This contribution adds to the literature on the regulation of crypto finance; moreover, it also adds to the comparative law literature, looking at the sources and dynamics of divergence in the regulation of innovative technologies.

The chapter focuses on the comparative regulation of two specific crypto assets, cryptocurrencies and stablecoins, but it can also be used to approach other crypto-assets. The analytical framework consists of three steps: (1) defining the economic function of different crypto-assets; (2) investigating the—potentially divergent—goals pursued by regulators; (3) analysing the rule-making strategies and the legal tools employed by regulators against the economic function of the regulated crypto asset and the regulatory goals.

To define the economic function of crypto-assets, it is crucial to functionally define the form of ‘financial disintermediation’ of different crypto-assets. Crucially, the industry and regulatory hype for ‘financial disintermediation’ hides a re-intermediation process, where a variety of new ‘crypto’ intermediaries, such as exchanges, wallets, developers and the blockchain infrastructure itself, aims at replacing old intermediaries.

On the one hand, cryptocurrencies can be defined as digitally scarce units of value the properties and circulation of which are prescribed via computer code. In this framework, cryptocurrencies are defined broadly and encompass crypto-assets designed as a means of payment and alternative investment opportunity, such as Bitcoins, native currencies supporting wider blockchain platforms such as Ethereum as well as crowdfunding schemes based on blockchain protocols, such as the thousands of initial coin offerings (ICOs). All these assets are volatile by design and are traded in centralized or decentralized crypto exchanges. Functionally, they resemble instruments commonly used in the capital markets and aim at substituting those. It is beyond the scope of the chapter and of this blogpost to engage in the discussion on whether cryptocurrencies should be legally qualified as securities, but the functional resemblance is clear and stems from the theory of financial intermediation.

On the other hand, stablecoins are a subset of cryptocurrencies whose aim is to maintain a stable value, usually referencing the US Dollar, ie, 1 coin is worth \$1. Stablecoins, despite being a ‘sub-category’ of cryptocurrencies, are different as the existence of a stabilization mechanism allows them to generate an expectation of safety and liquidity in stablecoin holders.

Performing different functions in the crypto economy, cryptocurrencies and stablecoins require different regulatory regimes. This leads to the second step of the framework, investigating what the regulator should functionally achieve. In finance, regulators typically aim at promoting market efficiency, protecting investors and safeguarding financial stability. These goals cannot necessarily fully co-exist, and different regulators may decide to prioritize these goals differently. Typically, in capital markets investor protection is prominent, whereas in banking safeguarding financial stability is considered the cornerstone of the regulatory framework.

Regarding crypto-assets, regulators should aim to make sure that these are allocated to those who value them the most or, in other terms, that the market properly works. Blockchain technology promised to perform this task without the need for intermediaries or regulation; however, there is now ample evidence that this promise has not been kept. Therefore, one can expect regulators to try and promote market efficiency by lowering barriers to entry, increasing legal certainty, and protecting investors with disclosure, obligations and conduct of business rules. The two goals are not necessarily compatible, and trade-offs exist.

In contrast, stablecoins raise specific concerns in terms of liquidity risk and monetary sovereignty, issues that are typically linked to banking; hence, the financial stability aspect should be prominent. Consequently, one should expect a more rigorous approach to licensing and quantitative and qualitative requirements on stablecoin issuers.

Third, policymakers must decide how to pursue these goals. From a comparative perspective, this is the step where regulators take the most divergent paths. Different regulatory regimes are not only explained by different economic functions and different goals pursued by the regulators, but also by other contextual factors, such as different regulatory cultures, willingness to engage in regulatory competition, and the effect of industry lobbying. All these factors influence the rule-making strategy and the regulatory tools employed.

In a fast-evolving field such as crypto assets, regulatory strategies diverge sharply, revealing different ways in which regulatory goals are prioritized and other contextual features shaping divergent regulatory approaches. The paper identifies two macro-categories: corner and internal solutions.

Corner solutions are, for instance, the ban of all crypto activities, as decided by China or, on the other side of the spectrum, the decision to provide

cryptocurrencies with ‘legal tender’ status, as in the case of El Salvador. So far, these corner solutions have proved ineffective.

The paper discussed three main ‘interior’ rule-making strategies: building a completely new regime that specifically applies to crypto activities; explicitly referring to existing regulatory regimes; and taking an enforcement-driven approach where existing regulatory agencies compete for interpreting their mandate and current regulation expansively. These three approaches have been followed, respectively, by the European Union with its Market in Crypto Assets Regulation (MiCA); the United Kingdom with the Financial Service and Market Act (FSMA); and the United States where the SEC and CFTC demonstrated a high level of activism in the crypto sphere. This is partly the result of the agency infrastructure of the US financial regulatory landscape and of the prolonged inability of the federal legislator to pass a comprehensive law.

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