Digital Currencies
Governance Group

Redemption of Asset-referenced Tokens

DCGG Position Paper

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As a representative of issuers and service providers of crypto-assets, the Digital Currencies Governance Group (DCGG) welcomed the European Commission's proposal for Markets in Crypto Assets (MiCA) Regulation and the clarity and harmonised rules it will bring to the crypto-assets sector.

However, based on the Commission's proposal and the General Approach (GA) reached by the Council of the European Union (Council), we see a couple of **major issues that would prove to be detrimental for a large section of the crypto-assets sector and contradictory to the stated objectives of the MiCA Regulation**. These concerns are primarily related to the **potential prohibition on redemption fees for asset-referenced tokens (ARTs) and e-money tokens (EMTs)** and **the restriction of consumer rights associated with redemption.**

Issue 1: The prohibition of redemption fees for ARTs would invalidate the entire business model of most ARTs and commodity-referenced stablecoins:

- According to Article 35(4b) of the GA on MiCA, the Council states that the redemption of ARTs shall not be subject to a fee without prejudice to wind-down or recovery plans.
- The core business model of many ARTs issuers requires charging fees for the redemption of their products in order to compensate for the cost of securely issuing and managing the tokens.
    - For example, for an ART solely referenced to commodities such as Tether Gold (XAUt), costs are incurred in the actual delivery of the referenced asset which is physical gold. Additionally, XAUt does not charge transfer (gas) fees on its tokens, meaning the redemption fee it charges is a primary source of recovering cost for the company. The purpose of XAUt is to give holders direct exposure to gold, hence it does not offer redemption in fiat currencies.
- Thus, it would severely limit the development of the crypto-assets sector in the EU as well as the EU's position as a leader in crypto-asset regulation.
- Commodity-referenced stablecoins are typically redeem directly for the physical commodity, as such, a redemption fee is necessary to cover costs related to the physical delivery of the referenced asset.
- Other more traditional financial products offered by investment firms, fund managers, and brokers charge fees on the products and services they offer to customers, which is inconsistent with the banning of redemption fees for crypto assets used as an investment product by consumers, such as ARTs

- Prohibition of redemption fees goes against precedent established in previous legislation such as Article 23(1i) of the Alternative Investment Funds Managers Directive (AIFMD), which allows fees on AIFs to be set.
- Most investment funds charge a redemption fee for redeeming shares of a fund, and in this particular aspect, ARTs are not different as a product.

Solution: DCGG supports the original text of the Commission proposal regarding redemption fees and as the best way forward. Article 35 of the Commission's proposal for MiCA states that the issuers of ARTs shall establish a policy setting out, among other things, the fees applied when the holder of an ART exercises their redemption rights. The original text also states that the fees must be proportionate and commensurate in relation to actual costs incurred by the issuer. Allowing for issuers of both ARTs and EMTs to charge redemption fees not only allows for the development of more vibrant EU crypto-assets industry, but also treats them fairly in relation to their traditional finance counterparts.

Issue II: Redemption rights requirements on ARTs are incompatible with the redemption process for commodity-referenced stablecoins

- DCGG is concerned that there is a risk that the text of the proposal could be interpreted to mean that issuers of ARTs should grant holders redemption rights near immediately and ensuring the redemption of the ARTs at market value within a very limited period of time.
- This restriction severely limits the diversity of current or potential products which consumers can receive from ART issuers.
- Since the redemption of certain ARTs depends on meeting specific criteria such as time or thresholds of tokens being held, it should be clearly and firmly stated that the issuers should be able to specify their criteria for redemption.
- The rights for redemption should take into account the types of assets being referenced by the ART – so long as they are clearly stated to investors.
- For example:
    - In the case of ARTs solely referenced to commodities such as XAUt, redemption of the tokens can only be offered once the holder has an amount that equals the weight of one London Good Delivery gold bar, thus making it impossible for the issuer to redeem at any time as it holds all reserves in gold.
    - Requiring a token like XAUt to be redeemable at any time for market value would mean holders could demand that their standard gold bar be divided to match the number of tokens they want to redeem, thus creating issues with the tracking for the gold that has been redeemed.
    - The physical delivery of gold for the redemption of tokens takes time due to the limitations around the delivery of a precious metal to a specific location for a holder to retrieve and

would incur costs which need to be covered. This means that the redemption of XAUt immediately would be physically impossible.

Solution: DCGG supports the original proposal of the European Commission on MiCA as the best way forward regarding redemption rights. Article 35(2a) of the original proposal states that where holders of ARTs are granted redemption rights, the issuer of the ART shall establish a policy setting out, among other things, the conditions, including threshold, periods, and timeframes, for holders of ARTs to exercise their redemption rights. This would allow issuers of ARTs to have the flexibility they need to allow for redemption based on the time and threshold considerations of the assets backing their tokens. Limiting this capability of issuers would disincentivise commodity-referenced token issuers from seeking to operate in the EU.