

Blockchain Advisory Limited

# DLT FRAMEWORK

Frequently Asked Questions



Blockchain  
Advisory

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## Introduction to Malta

Malta enjoys a stable political climate with accredited economic growth higher than most EU countries and thus, is guaranteed to be a safe hub from which to operate one's business. Additionally, being part of the Commonwealth, a member of the EU since 2004 and part of the Schengen area since 2007, has aided Malta to promote itself as a hub which provides a perfect platform for trade and free movement.

Malta does not only guarantee safety and stability to those wishing to operate their business from Malta, but provides a forum within which a whole ecosystem is in place to support the growth and emancipation of one's business. From direct government support to attractive tax incentives, Malta has, time and time again, proven to be one of the leading jurisdictions for business ventures to thrive.

Indeed, Malta has never shied away from being first with regards to regulating various prominent industries. In this respect, the best success story has been that of the remote gaming industry, where Malta was the first country in the world to regulate such industry back in 2004. With its first mover advantage and a robust regulatory framework in place, Malta became a reference point for all other jurisdictions, with various jurisdictions just starting to take the first steps towards regulating the remote gaming industry, fourteen years after Malta had set the standard.

Malta is determined to achieve the same success in the distributed ledger technology (DLT) industry, and indeed, aims to live up to the expectations of becoming the world's 'Blockchain Island'. With various notable benefits in its arsenal, Malta has opened its doors wide to influential, established businesses and promising start-ups alike, following the setting up a welcoming regulatory framework which simultaneously incentivise business growth and affords protection to the participants of the same ecosystem.

## The regulatory framework – a summary

## The regulatory framework – a summary

As from the 1st of November 2018, the new framework regulating DLT technology was promulgated. This entailed the introduction of three Acts covering the fundamental aspects underpinning this ever-changing and innovative industry.

Several jurisdictions have been, to a greater or lesser extent, working towards embracing DLT and participants therein. Over the past two years, most of the business and regulatory focus has been on cryptocurrencies and crypto-assets issued on top of blockchains, as well as initial coin offerings (ICOs), a recent fintech phenomenon whereby an entity can issue its own cryptocurrency or crypto-asset in exchange for other cryptocurrencies such as Bitcoin and Ether. ICOs, in fact, have been used to collect funds amounting to more than two billion U.S. Dollars in 2017 alone. To date, the most active jurisdictions especially vis-à-vis ICOs have been Singapore, Switzerland, and Estonia. None of these jurisdictions, however, possess a holistic regulatory framework covering ICOs and other applications or uses of DLT, which is where Malta enters the scene.

### The Acts essentially cover three core aspects:

- (i) the Malta Digital Innovation Authority (MDIA) Act (Chapter 591 of the Laws of Malta) covers the establishment of a regulatory authority, called the Malta Digital Innovation Authority (MDIA), dedicated towards the supervision and certification of DLT platforms and smart contracts, which are referred to as technology arrangements under the said Act;
- (ii) (ii) the Innovative Technology Arrangements and Services (ITAS) Act (Chapter 592 of the Laws of Malta) covers the setting-up of a registration & certification mechanism for any technology arrangements which voluntarily decide to register themselves as such, which technology arrangements shall be certified by approved Systems Auditors; and
- (iii) (iii) the Virtual Financials Assets (VFA) Act (Chapter 590 of the Laws of Malta) lays out a financial instruments test for all so-called DLT assets, ergo cryptocurrencies, and determine whether such DLT assets fall under existing Maltese and/or EU regulation, therefore potentially having them classified as financial instruments or e-money, whether it classifies as a virtual token, ergo a pure utility token, meaning it would fall

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<sup>1</sup> Namely, the Markets in Financial Instruments Directive II (MiFID II), and the Investment Services Act which transposed MiFID II into Maltese legislation. The E-Money Directive is another legislative act which is taken into consideration since a DLT Asset may also be classified as e-money.

## The regulatory framework – a summary

(continued)

outside the scope of any applicable legislation, or a new fourth category, that of virtual financial assets, which would be caught under the aforementioned VFA Act.

This three-pronged approach places Malta in a very favourable position when compared to its peers, mostly due to the creation of the MDIA, which is the first regulatory authority of its kind in the world. The MDIA serves as a seal of quality for any DLT-based platforms or applications, separating the wheat from the chaff. The voluntary nature of any applications by those constructing DLT-based platforms ensures that any development taking place in Malta is not stifled, and only those who wish to obtain regulatory approval would be invited to tender their applications and submit themselves to regulatory and technical scrutiny. System auditors need not be based in Malta and can operate through resident agents, meaning that the doors are open for anyone with a legitimate interest in aiding the regulatory framework covering DLT-based projects.

The new legislative framework under the VFA Act under supervision of the Malta Financial Services Authority (MFSA) gives further security to investors and platform developers & issuers alike vis-à-vis the ICO offering at hand and the listing of DLT assets on crypto-exchanges, now known as VFA exchanges under the VFA Act. The financial instruments test ensures that any cryptographic token issued during the ICO stage, or listed on a crypto-exchange, would either be within the confines of existing regulation or not. This is the cause of frustration for most entities seeking a jurisdiction within which to launch and run an ICO due to the regulatory uncertainty, which uncertainty leads to an unstable environment for business. The Maltese VFA framework sought to eliminate such uncertainty and provide the perfect legal ecosystem for both established companies as well as up and coming start-ups to thrive and prosper without stifling innovation.

## Virtual Financial Assets Act (VFAA) – FAQs

### 1. What does the VFAA cover?

The VFAA covers the issuance of DLT assets through an ICO, token generation events, or other similar events which need not necessarily involve the collection of funds; the DLT assets need to qualify as virtual financial assets in order to fall within the remit of the VFAA. The VFAA also covers VFA services, namely the following:

- The reception and transmission of orders for buying/selling/subscribing to VFAs;
- Execution of orders on behalf of other persons;
- Dealing on own account i.e. against proprietary capital;
- Portfolio management of third parties;
- Custodian or nominee services;
- Investment advice in a professional capacity;
- Placing of VFAs to specified persons and that are not admitted to trading on a VFA exchange; and
- The operation of a VFA exchange.

### 2. How does one apply for a license under the VFAA?

One can apply for a license under the VFAA, for the abovementioned activities, through a VFA Agent. Blockchain Advisory has already notified the MFSA on its intention to register as a VFA Agent and can assist any interested parties requesting any of the aforementioned VFA services. The VFA Agent has various responsibilities under the VFAA, and needs to be an advocate, accountant, auditor, or any other person holding the required authorisations, qualifications, and experience deemed by the MFSA to constitute adequate expertise.

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<sup>2</sup>“DLT asset” means: (a) a virtual token; (b) a virtual financial asset; (c) electronic money; or (d) a financial instrument that is intrinsically dependent on, or utilises, Distributed Ledger Technology.

<sup>3</sup>“virtual financial asset” or “VFA” means any form of digital medium recordation that is used as a digital medium of exchange, unit of account, or store of value and that is not - (a) electronic money; (b) a financial instrument; or (c) a virtual token.

## Virtual Financial Assets Act (VFAA) – FAQs (continued)

### 3. What are the different license categories/classes for VFA Service Providers?

Class	Services	Initial Capital Requirement (to be held by the Licensee)
1	Licence holders authorised to receive and transmit orders and/ or provide investment advice in relation to one or more virtual financial assets and/ or the placing of virtual financial assets. Class 1 Licence Holders are not authorised to hold or control clients' money.	EUR 50,000 (or EUR 25,000 & Professional Indemnity Insurance coverage)
2	Licence holders authorised to provide any VFA service but not to operate a VFA exchange or deal for their own account. Class 2 Licence Holders may hold or control clients' money in conjunction with the provision of a VFA Service.	EUR 125,000
3	Licence holders authorised to provide any VFA service but not to operate a VFA exchange. Class 3 Licence Holders may hold or control clients' money in conjunction with the provision of a VFA Service.	EUR 730,000
4	Licence holders authorised to provide any VFA service. Class 4 Licence Holders may hold or control clients' money in conjunction with the provision of a VFA Service.	EUR 730,000

### 4. Which type of crypto-exchanges will be covered under the VFAA?

Both crypto-to-crypto and fiat-to-crypto exchanges will be covered under the VFAA. However, if the exchange is handling fiat currency deposits directly, rather than through approved payment service providers, then it would require the necessary license under MiFID II along with the license under the VFAA.

### 5. Can a VFA exchange trade financial instruments as well?

If an exchange wishes to trade both VFAs as well as financial instruments, such as security tokens, it would need to obtain a separate license, using a separate corporate entity, under the Investment Services Act.

### 6. Can I offer the ICO or VFA service only to Maltese residents?

No, you can offer the ICO or VFA service in any other jurisdiction where such an activity is not prohibited or regulated in a ring-fenced manner. This would mean that the offering of a VFA in an ICO, for example, can be made in any country where ICOs are not prohibited or already regulated. On the contrary, the offering of security tokens can only be made in each and every jurisdiction where the applicable license or concession is obtained, since security tokens are already regulated in most jurisdictions.

## Virtual Financial Assets Act (VFAA) – FAQ (continued)

## The MDIA Act and the ITAS Act – FAQ

### 7. What do I need to do to run an ICO?

You would need to do the following:

- a) Set up the required legal entity, such as a company, to conduct the ICO;
- b) Obtain a legal opinion from a Malta-warranted advocate, later on with such person being a licensed VFA Agent, stating that the token being offered is not a financial instrument;
- c) Draw up a whitepaper which is compliant with the First Schedule of the VFAA;
- d) Appoint a Systems Auditor, VFA Agent, Custodian, Financial Auditor, and Money Laundering Reporting Officer; and
- e) Conduct the ICO in line with the VFAA and relevant obligations.

### The MDIA Act and the ITAS Act – FAQ

The reason why both the MDIA Act and the ITAS Act will be dealt with together is because both are reliant on one another; the MDIA Act covers the set-up and structure of the MDIA, while the ITAS Act covers the technical requirements and the set-up of system auditors.

#### 1. Will the MDIA replace other regulatory authorities?

No – the MDIA will complement other authorities such as the MFSA, the Malta Gaming Authority, the Malta Communications Authority, and so on. It will provide its technical assistance in any matter as required by such other authorities.

#### 2. Do I need to register with the MDIA whenever developing anything in relation to blockchain technology?

No – registration with the MDIA is completely voluntary. However, it is recommended to have one's platform audited and certified by the MDIA as it will serve as an official regulatory stamp of approval. The only instance where certification from the MDIA may be mandated is if a separate regulatory authority, such as the MFSA or the MGA, require such certification.

#### 3. How will the auditing process work?

The audit of the DLT platform or application, known as a technology arrangement under the said Acts, will be conducted by third party system auditors approved by the MDIA. The system auditors can be located both within Malta as well as within any EU/EEA state. Blockchain Advisory shall be offering such.

## The MDIA Act and the ITAS Act – FAQs (continued)

### 4. What are the requirements to have a technology arrangement certified under the ITAS Act?

The requirements are various as listed under the First Schedule of the ITAS Act. The technology arrangement shall be considered as such if it meets one or more of the following criteria:

- i. software and architectures which are used in designing and delivering DLT which ordinarily, but not necessarily: (a) uses a distributed, decentralized, shared and, or replicated ledger; (b) may be public, private or hybrids thereof; (c) is permissioned, permissionless or hybrids thereof; (d) is immutable; (e) is protected with cryptography; and (f) is auditable;
- ii. smart contracts and related applications, including decentralised autonomous organisations (DAOs) as well as other similar arrangements;
- iii. any other innovative technology arrangement which may be designated by the Minister, on the recommendation of the Authority, by notice from time to time. Moreover, the technology arrangement needs to appoint both an administrator and a technical administrator and the term of validity of such certification is for a period of 2 years.

### 5. Are any other service providers covered under the ITAS Act?

Apart from administrators and technical administrators, technology service providers are covered under the ITAS Act. Technology service providers are classified as such if they offer the following:

- a) the review services referred to in the ITAS Act with reference to innovative technology arrangements provided by system auditors;
- b) the technical administration services referred to in the ITAS Act with reference to innovative technology arrangements provided by technical administrators.

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“administrator” means an officer or any person who is appointed to carry out representative and fiduciary functions in the control and administration of a legal organisation, and any person who carries out such functions even if under another name.

“technical administrator” means the person who, upon a written engagement accepts to carry out specific functions relating to the operation, of the whole or a designated part, of the system as are established in the ITAS Act, in guidelines issued by the MDIA, as the same may be supplemented by the conditions applicable to the certification of the particular certified technology arrangement.



## Other facts about Malta

- Malta has been chosen as a base of operations by various prominent companies in the blockchain space such as Binance, OKEx, Bittrex, Bitfury, Waves and others.
- Tim Draper himself has endorsed Malta and claimed that it has a big lead over other jurisdictions due to its efforts in the blockchain space .
- Two of the largest blockchain events in Europe, Delta Summit & Malta Blockchain Summit, took place in Malta which brought together the main industry players, investors, local service providers and professionals.
- Two blockchain and crypto associations – Bitmalta and Blockchain Malta Association.
- University of Malta and Malta Information Technology Authority (MITA) have partnered to set up a €300,000 blockchain and DLT focused scholarship fund

## Tax and Operational regime

- Malta offers an attractive EU approved tax regime combining a system of tax refunds and a headline tax rate which results in an advantageous overall effective tax rate.
- A bank account from another jurisdiction may be used for the operations of the company.
- No need for physical presence for the actual registration of the company.
- No requirement for local resident partners/shareholders.
- No withholding taxes on outbound remittances of dividends, interest or royalties.
- No stamp duty or income tax on gains made on disposal of shares in Maltese companies by non-residents.
- Tax incentives for highly qualified personnel operating in specific industries.

## Business Jurisdiction in General

- GDP growth up to 5.4% in 2018 making it the second best rate in Europe .
- Robust financial services sector.
- Attractive citizenship, residence and key employee programmes aimed at facilitating international mobility of families and employees.
- One of the least affected EU member states in the 2008-2012 recession.
- Double-tax treaties with a large number of EU and non-EU jurisdictions

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<sup>6</sup> <http://www.independent.com.mt/articles/2018-05-22/local-news/Malta-has-big-lead-over-other-countries-due-to-proposed-blockchain-regulatory-framework-Tim-Draper-6736190322>

<sup>7</sup> [https://ec.europa.eu/info/business-economy-euro/economic-performance-and-forecasts/economic-performance-country/malta/economic-forecast-malta\\_en](https://ec.europa.eu/info/business-economy-euro/economic-performance-and-forecasts/economic-performance-country/malta/economic-forecast-malta_en)



**Blockchain  
Advisory**

**Blockchain Advisory Limited**

The Penthouse, Suite 2,  
Capital Business Centre,  
Entrance C, Triq taz-Zwejt,  
San Gwann SGN 3000,  
Malta. EU

t: +356 2163 7778  
e: [info@bca.com.mt](mailto:info@bca.com.mt)  
[www.bca.com.mt](http://www.bca.com.mt)