April 29, 2024

Ms. Verena Ross
Chair
European Securities Markets Authority

Submitted via www.esma.europa.eu

Dear Madam,

Public response to ESMA's consultation on reverse solicitation under MiCA

The Institute of International Finance (**IIF**) welcomes the opportunity to publicly respond to the European Securities and Markets Authority's (**ESMA's**) consultation report containing proposed guidelines concerning the reverse solicitation exemption under Article 61 of the Markets in Crypto-Assets Regulation (**MiCA**).

General comments

In engagements with global and select national regulators on crypto-assets prudential and conduct of business issues, we have consistently advocated for a measured approach that does not unduly restrict the ability of regulated financial institutions to prudently engage in crypto-asset activities, such that associated risks will be subject to robust sound risk management practices.[1] We have also advocated for an appropriately calibrated capital and disclosure regime that would support responsible adoption of novel technologies in the financial markets by helping to improve the confidence of investors and the wider market around this developing asset class.

We would encourage an approach to regulation that recognizes the dynamic nature of this asset class and supports a framework designed to evolve in line with its development. Recommendations for crypto-asset markets should not be more prescriptive or restrictive, proportionate to the risks they present, than regulation of traditional financial asset markets.

We continue to strongly advocate for technology neutrality as a guiding principle for regulation in this area, and support the principles of "same risk, same regulatory outcome" and "same asset, same risk".

Regulatory equivalence

We would urge the importance of establishing a formal equivalence regime for crypto-asset and stablecoin services, particularly between major financial jurisdictions. Such regimes are essential in traditional financial services (for example, under MiFID 2 and EMIR), and are similarly essential in crypto-asset markets that are by their nature global and interoperable. We note that an assessment of whether an equivalence regime should be established for entities providing crypto-asset services and for issuers of asset-referenced and e-money tokens from third countries is due to be made by

[1] See our October 4, 2022 joint response to the Basel Committee on Banking Supervision (**BCBS**) on the prudential treatment of crypto-asset exposures, our December 15, 2022 response to the Financial Stability Board's consultation on crypto-assets and stablecoins, our July 31, 2023 response to the International Organization of Securities Commissions on crypto and digital asset markets, and joint February 1, 2024 response to the BCBS on disclosure of cryptoassets exposures. See also our April 30, 2023 response to the UK Treasury's consultation on the future financial services regulatory regime for cryptoassets.

the Commission by mid-2025 under Article 140(2)(v) of MiCA. We note that this equivalence regime is critical and recommend it align as closely as practicable to MiFID 2.

Specifically, and responding to this consultation, it is not clear why firms that are equivalently regulated in third countries (including adjacent economies such as the UK and Switzerland) should be treated as if they were wholly unregulated for these purposes. To do so would be to impose regulatory and market fragmentation among even advanced economies that enjoy broadly comparable levels of regulation and supervision. We note that MiFID 2 has both an equivalence regime and a broad reverse solicitation exemption; the two concepts are certainly independent and the reverse solicitation exemption from authorisation is not required for firms authorised under regimes that are assessed as equivalent.[2]

Other regimes are in place beyond Europe, including in Singapore, Hong Kong SAR and Dubai, to name a few. As for the U.S., a combination of Federal securities and commodities regulation and State-based money transmitter licensing, special-purpose licensing, and trust company licensing, has allowed the development of a very sophisticated digital finance ecosystem with broadly positive consumer outcomes. As major developing countries like Brazil and India put together their crypto-asset regulatory regimes, the EU's signaling here will be impactful in either encouraging or discouraging an open and interoperable regulatory regime versus one that is unduly closed off or protectionist. Openness and interoperability will ultimately benefit EU-based businesses and further regimes may take direction from MiCA's early establishment. At present, the draft appears not to consider the signal it sends to economies around the world to practice protectionist policies.

Best practice regulation

We respectfully raise concern with ESMA's methodology on this issue and suggest that it is problematic for the EU Digital Agenda. We recognize that reverse solicitation is not a new concept in EU law; however, we are still concerned that these proposals have been put forward with little accompanying analysis or attempt to quantify their impact. We suggest that some cost–benefit assessment should be done to ground ESMA's recommendations. In this regard, the opportunity cost of EU-based consumers and platforms being unable to access global liquidity pools needs to be taken into account.

Overall, the current draft appears predisposed to close the gate left open in Article 61 as much as possible. We observe that the questions in the current draft all appear to lean towards further tightening, and there are no questions that ask whether the proposals are too restrictive. Moreover, the introductory text reframes reverse solicitation as a "prohibition" rather than an "exemption". A starting point that aims to ensure that EU consumers have a right to choose among a range of financial services product providers would seem more appropriate.

Opportunity cost concerning global liquidity

We respectfully question the conclusion that the proposals do not create "new costs for concerned market stakeholders beyond those that naturally stem from the obligations in MiCA." It is unclear whether the opportunity costs arising from as strict and onerous a regime as is proposed, not only for EU investors but also for those EU-based crypto-asset service providers (CASPs) that may wish to route liquidity or orders onto non-EU based platforms with client consent, have been identified and taken into account.

[2] We note that for retail and elective professional clients, a national authority has the discretion to require the third-country firm to establish a branch within its territory - this is subject to certain conditions for the firm as well as for the third country. For professional clients and eligible counterparts, cross-border activity is possible without establishing a branch, provided that the firm registers with ESMA and informs its clients that it is not subject to EU supervision - among other conditions, this requires a positive Commission equivalence decision. (See Equivalence decisions under MiFID II/MiFIR and PSD2 Regulatory Technical Standards on Strong Customer Authentication and Secure Communication (europa.eu) at p. 2)

Crypto-asset markets are global in nature, so maintaining local investor access to global liquidity is important; consideration of the opportunity cost of global liquidity is also necessary. While providing adequate consumer protection, local authorities should bear in mind the risk of effectively requiring local customers – and CASPs that service them – to use less liquid local venues. In economic terms, of course, the best consumer protection is provided by guaranteeing ongoing access to the deepest liquidity pools with the tightest spreads as illustrated by historical precedent, so long as client assets are adequately preserved. Regulatory protectionism threatens this by fragmenting liquidity.

The consideration of a tighter approach to reverse solicitation for crypto-asset services and activities should be balanced against the benefit to EU consumers of having access to products and services from well-regulated, established firms, including those located outside of the EU.

Against that background, we address each of the consultation questions in turn.

Q1: Do you agree with the approach chosen by ESMA? Do you see any potential loophole that could be exploited by third-country firms to circumvent the MiCA authorisation requirements?

Definitions

The draft guidelines contain several highly restrictive requirements, most notably, a very broad interpretation of solicitation that includes all brand advertising (including by way of sponsorship deals), even where there is no connection with crypto-assets and services, but also "participations in road shows and trade fairs."[3] This is likely to deter established financial services firms from being able to respond to an EU client request regarding any crypto-asset product or service to EU consumers in the future to avoid interrupting their ability to market their brand or other services to the entire EU market. Furthermore, the mere attendance of a third-country firm representative at a trade fair as an indication of solicitation could restrict ordinary pre-market entry activities – where it is customary for firms to use trade fairs to gage the market prior to considering entry – and thus seems to be an overstretch, be unfounded in practice, and create an undue presumption of solicitation.

The guidelines as drafted would require a very different onboarding workflow for EU clients of third-country firms. It is possible that third-country firms will be reluctant to build such an onboarding workflow and will in practice wall themselves off from EU consumers altogether (e.g. by geoblocking them). In our view, this will not be to the benefit of EU consumers and will also frustrate the EU consumer who would like to "initiate at its own exclusive initiative the provision of a crypto-asset service or activity by a third-country firm" in accordance with Article 61(1) of MiCA.

While policymakers have an understandable ambition that EU consumers interact with firms authorised in the EU, some consumers will also want to engage with non-EU firms, particularly if they offer products or services that those authorised at any point in time in the EU may not yet provide. There is a clear investor protection case for those interactions to be with a well-regulated third-country financial services provider, rather than those operating under limited or no regulation. For this realistic case, this requires adapting the guidelines to address established financial services firms with multiple business lines and whose brand is not predominantly associated with crypto-assets or services.

Languages

The proposed guidelines contain a presumption that having a website in an official language of the Union – and which is not "customary in the sphere of international finance" – should be a strong indication that a third-country firm is soliciting clients established or located in the Union. While language would presumably be considered in combination with a range of other indicators, we would caution that this strong indication not jump to conclusion too quickly, most affecting those

[3] Section 5.1, paragraph 12.

third-country financial services providers that have strong links with EU countries because of their diversified and international footprint, or are situated in countries that share cultural and language roots with the EU. Taken together with ESMA's broad interpretation of solicitation, this may discourage the provision of services in scope of MiCA by any third-country institution with a local language website, while not restricting third-country providers with no links to local communities whose website is in English or another "language of international commerce."

Incidentally, more clarity is needed on what languages count as a "language of international commerce."

Person soliciting

While we agree with aspects of the approach proposed by ESMA, we suggest clarifying in Guideline 2 that "solicitation … carried out … by any other person acting … implicitly on behalf of the third-country firm" would not include instances where a third party interacts with EU prospects beyond the reasonable control of the third-country firm and/or in breach of any contractual obligations between the third party and the firm.[4]

Q2: Are you able to provide further examples of pairs of crypto-assets that would not belong to the same type of crypto-assets for the purposes of Article 61 of MiCA? Or are you able to provide other criteria to be taken into account to determine whether two crypto-assets belong to the same type?

No comment.

Q3: Do you consider the proposed supervision practices effective with respect to detecting undue solicitations? Would you have other suggestions?

The supervisory monitoring tools suggested in 6.1 of the proposed Guidelines are disproportionate and excessive and have a starting assumption that firms adopting certain practices (local email or website addresses) are doing so in order to conduct prohibited activities. It should be clarified that a suspicion of wrongdoing (based on reasonable grounds) should be the determinant for investigating a firm.

Scope of level 1 mandate

MiCA Article 61(1) states that the reverse solicitation exemption applies to a "relationship" between a client and a firm, which by definition can be an ongoing and long-term client relationship (as opposed to a one-off service). The draft Guidelines, however, set out that the exemption can only be used for a very short period of time. The possibility of having an ongoing relationship should therefore be reflected in the guidelines.

The IIF and its members stand ready to engage in additional discussions and consultations on these topics, or to clarify any aspect of our submission. We thank you again for the opportunity to contribute to this important consultation.

Yours sincerely,

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Managing Director, Digital Finance

Andres Portilla
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[4] This could be the instance where a finder, appointed by the third-country firm to refer prospects who reached out to the finder to be linked with the third-country firm effectively solicits EU prospects, despite strict covenants on the scope of permissible activities.