APRIL 2024

ESMA CONSULTATION PAPER ON THE DRAFT GUIDELINES ON REVERSE SOLICITATION UNDER THE MARKETS OF CRYPTO-ASSETS REGULATION (MICA)

AFG's response

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The AFG federates the asset management industry for 60 years, serving investors and the economy. It is the collective voice of its members, the asset management companies, whether they are entrepreneurs or subsidiaries of banking or insurance groups, French or foreigners. In France, the asset management industry comprises 680 management companies, with €4355 billion under management and 85,000 jobs, including 26,000 jobs in management companies.

The AFG commits to the growth of the asset management industry, brings out solutions that benefit all players in its ecosystem and makes the industry shine and develop in France, Europe and beyond, in the interests of all. The AFG is fully invested to the future.

GENERAL COMMENTS

To begin with, we appreciate ESMA's proactive step in establishing criteria for reverse solicitation within the framework of the regulation of the crypto asset market (MiCA). We anticipate that these criteria will serve to safeguard investors while promoting fair competition among participants in the European crypto asset market. Additionally, we hope that these criteria will help to minimize discrepancies in the interpretation of reverse solicitation across different jurisdictions.

However, we are apprehensive about the potential for an overly expansive interpretation of these criteria, particularly regarding the multitude of regulatory regimes governing reverse solicitation.

Under MiFID II, According to Article 42, *"where a retail client or professional client, within the meaning of Section II of Annex II, established or situated in the Union initiates at its own exclusive initiative the provision of an investment service or activity by a third-country firm, the third country firm is not subject to the requirements under Article 39 of MiFID II (Establishment of a branch)."*

Article 61-1 of the MiCA Regulation, which states that "*Where a client established or situated in the Union initiates at its own exclusive initiative the provision of a crypto-asset service or activity by a third-country firm, the requirement for authorisation under Article 59 shall not apply to the provision of that crypto-asset service or activity by the third-country firm to that client, including a relationship specifically relating to the provision of that crypto-asset service or activity*."

Article 18 of the European regulation on cross-border marketing of UCITS/FIAs (2019/1156) states

Article 18- Evaluation: (...) *By 2 August 2021 the Commission shall, on the basis of a consultation of competent authorities, ESMA and other relevant stakeholders, submit a report to the European Parliament and to the Council on reverse solicitation and demand on the own initiative of an investor, specifying the extent of that form of subscription to funds, its geographical distribution, including in third countries, and its impact on the passporting regime. That report shall also examine whether the notification portal established in accordance with Article 13(2) should be developed so that all transfers of documents between competent authorities take place through it.*

Finally, at French level, AMF Position 2014-04[1] clarifies the definition of the marketing in France of units or shares in UCITS and AIFs and describes the different regimes applicable to the marketing in France of such units.

As a result, if a service provider has both Investment Service Provider and CASP status, under which regime should it fall? The regime must therefore be unified to ensure consistency of rules.

Further, more specifically in the case of reverse solicitation, 3rd country based providers in the EU, of crypto assets with financial instruments characteristics, will likely “arbitrage" the reverse solicitation regime of MICA, with that of MIFID II, if the latter is left more lenient than MICAR.

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?

I. On the means of solicitation

When it comes to solicitation methods, ESMA proposes a comprehensive list detailing all the ways in which a third-country company could attract European customers, an approach that we at the AFG support. However, we believe that certain aspects require clarification.

ESMA outlines criteria for defining Reverse Solicitation, yet it lacks a clear definition of reverse solicitation itself. The criteria involving financial education or event invitations could potentially be used to bypass reverse solicitation rules for third-country digital asset service providers. For instance, an invitation to a social, sporting, training, or informational event serves as an initial step and an effective means of promoting the services of a third-party company to European prospects or customers. Likewise, the broadcasting of online commercial events organized or sponsored by a third-country company on any website, without geographical restrictions, serves as an indication of solicitation. The challenge arises in distinguishing between educational efforts devoid of promotion and those coupled with promotion.

When it comes to using an official EU language “customary in the sphere of international finance”, the concept remains open to debate, especially considering that certain languages have international usage, such as Spanish and Portuguese in Latin America, or French in Africa. Language, like other criteria, should be considered one of several indicators. It alone isn't enough to determine whether solicitation is active, but it can serve as a hint that, when combined with other criteria, may indicate solicitation.

[1] https://www.afg.asso.fr/afg-document/position-amf-n2014-04-guide-sur-les-regimes-de-commercialisation-des-opcvm-et-des-fia-en-france/#:~:text=La%20position%20AMF%20n%C2%B0,en%20France%20de%20ces%20entit%C3%A9s.

As an example, consider the combination of language and URL. More broadly, we advocate for the "bundle of clues" approach outlined in Article 721-1-1[2] of the RGAMF (General Regulation of French NCA) as the appropriate method. Furthermore, we assert that financial education providers within the European Union should be regulated under all circumstances.

II. On the notion of influencers with regard to persons soliciting

We observe that, as part of its effort to establish a broad interpretation of reverse solicitation, ESMA is suggesting the application of reverse solicitation to promotions carried out by influencers. We see this broadening as beneficial to prevent forum shopping, which currently disadvantages French, Italian, and Spanish participants, as the concept is narrowly defined in their respective jurisdictions. Primarily, we believe influencers should explicitly disclose whether they are being remunerated by indicating *"remunerated partnership."* Failure to do so should incur penalties.

The guidelines adopted should draw inspiration from the French law of June 9, 2023, aimed at regulating commercial influence and combating influencer abuses on social networks. This law provides a precise definition of this profession: individuals who, in exchange for remuneration or benefits, *"utilize their notoriety among their audience to disseminate"* online *"content aimed at promoting, directly or indirectly, goods, services, or any cause whatsoever."*

III. On the notion of solicitation carried out through general clauses

The criteria for qualifying as reverse solicitation are broader than those outlined in MiFID II but do not address a significant aspect of financial regulation: terms and conditions. In its public statement dated January 13, 2021, ESMA highlighted that "some firms appear to be attempting to bypass the requirements of MiFID II [...] by utilizing online pop-up boxes where customers declare that any transaction is carried out at the sole initiative of the customer."

We concur with the “factual” approach developed in § 18 by ESMA. However, while we understand that ESMA considers that reverse solicitation can be either contractual or non-contractual, as well as formal or informal (paragraph 15 and guideline 3), it is essential, given the issues raised during the implementation of MiFID, to explicitly mention acceptance in the terms and conditions. Furthermore, such consent cannot be blanket and encompass any future service, unless doing so would facilitate circumvention of the concept of reverse solicitation. This consent must not preempt consent for subsequently provided services: it must be clearly and explicitly expressed for each service, and for each

[2] https://www.amf-france.org/fr/eli/fr/aai/amf/rg/article/721-1-1/20210523/notes

operation within the same service. Definitions in the guidelines must be precise. *"Operation by operation*" should equate to *"transaction by transaction," "asset by asset."* To prevent dilution of the concept and to safeguard the European market and investors from external entities potentially exploiting more lenient or non-existent regulations regarding organization and security, overly generic acceptance of these concepts must be avoided.

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?

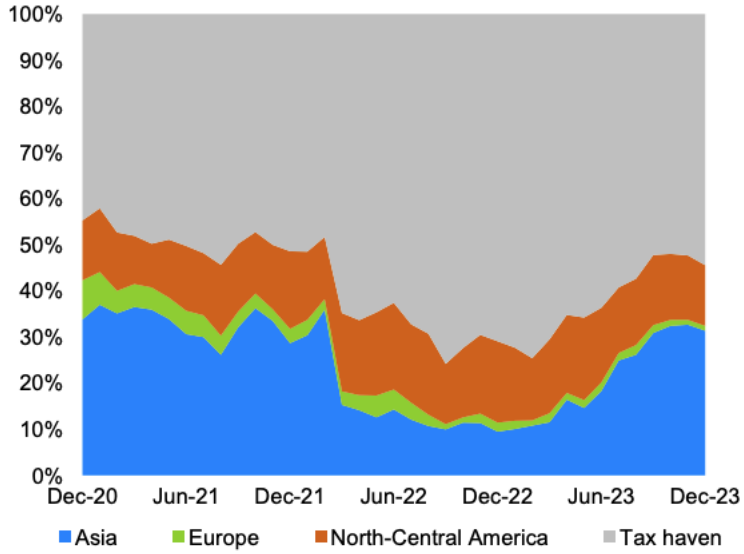
We advocate for interpreting the qualification of reverse solicitation in the broadest possible sense, encompassing any additional services offered and any educational services, regardless of the asset or service category. It is crucial for European Union (EU) regulations to take a less lenient stance towards third-country or unlicensed entities operating within the EU and offering purportedly "unregulated" services or activities, especially when they aim to enhance their brand or reputation. Actions undertaken in the Union from 2017 to 2024 appear to have been primarily aimed at acquiring new European users under the guise of training and educational initiatives, as highlighted in the latest ESMA TRV Risk Analysis report (ESMA50-524821-3153).

It is concerning to observe that, despite the European Union's position in the global economy and savings market, trading volumes on EU trading platforms are notably low, if not nonexistent. This situation suggests a significant lapse in effective investor protection within the Union, enabling the proliferation of entities employing circumvention tactics such as education and sports sponsorship to attract European offshore investors, without facing criminal or administrative penalties.

Chart 7

Trading volume by exchange domicile

Most crypto exchanges located in tax havens



Note: Share of monthly trading volume (in USD) by geographic location of the exchange headquarters. Location manually identified from publicly available sources.
Sources: Kaiko, ESMA.

We can also observe that the implementation of regulations aimed at safeguarding their markets by more developed geographical regions than the EU, notably the USA and Japan, has proven to be an effective measure in protecting their investors facing scandals involving FTX. In this regard, it should be noted that in the FTX case, investors in FTX US and FTX Japan were able to recover their funds due to asset segregation, as their jurisdictions had implemented very stringent rules prohibiting any form of solicitation, whether direct or indirect, explicit, or implicit, within their respective territories starting from 2021 and 2022. Conversely, in Europe, hundreds of thousands of retail investors were utilizing FTX.com, based in the Bahamas, where notably, no such segregation rules would apply.

Therefore, we would strongly encourage ESMA to evaluate the risks stemming from any excessively flexible approach to reverse solicitation of European investors by entities located in third countries. Notably, such an approach could potentially be exploited through seemingly non-commercial activities, thereby circumventing regulatory oversight.

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

The emergence of crypto assets and blockchain technologies has brought a significant innovation to the global financial landscape. Unlike traditional investment products, which are typically regionally focused, the services and instruments associated with crypto assets operate within a fully international and interconnected framework. This inherent characteristic of the crypto ecosystem raises concerns about the effectiveness of fragmented supervisory regimes within the European Union.

It is undeniable that national supervisory frameworks, often tailored for local financial markets, struggle to comprehend the complexity and scale of activities involving crypto assets. Furthermore, the varying regulatory approaches across the EU create potential loopholes in investor protection, leading to uneven treatment and unnecessary risks for investors based on their location or where market players operate or promote their services.

Given this context, it is crucial to consider the necessity of a centralized, unified approach to supervising crypto services and instruments within the EU. Such an approach would ensure a consistent level of protection for all European investors, foster innovation in the sector while maintaining financial stability, and enhance the EU's reputation as a global leader in regulating emerging financial markets.

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