RESPONSE TO CONSULTATIONS

MARKET IN CRYPTO ASSET

Guidelines on templates for explanations and opinions, and the standardised test for the classification of crypto-assets, under Article 97(1) of MiCAR

Luxembourg, 11 October 2024

The Association of the Luxembourg Fund Industry (ALFI) represents the face and voice of the Luxembourg asset management and investment fund community. The Association is committed to the development of the Luxembourg fund industry by striving to create new business opportunities, and through the exchange of information and knowledge.

Created in 1988, the Association today represents over 1,500 Luxembourg domiciled investment funds, asset management companies and a wide range of business that serve the sector. These include depositary banks, fund administrators, transfer agents, distributors, legal firms, consultants, tax advisory firms, auditors and accountants, specialised IT and communication companies. Luxembourg is the largest fund domicile in Europe and a worldwide leader in cross-border distribution of funds. Luxembourg domiciled investment funds are distributed in more than 70 countries around the world.

We thank the European Supervisory Authorities (EBA, EIOPA and ESMA) (ESAs) for the opportunity to participate in this consultation on the proposed Guidelines on templates for explanations and opinions, and the standardised test for the classification of crypto-assets, under Article 97(1) of MiCAR.

Our members appreciate the opportunity to share the views of the market practitioners in Luxembourg, with regards to classification of crypto assets, in the context of MiCAR.

In order to provide evidence of the industry considerations with regards to those various topics in the context of MiCAR, answers will be provided, focusing on priorities stemming from industry-related consideration and impact assessment. Some response elements will also reiterate previous considerations, raised in the context of the previous ESMA consultation on guidelines on conditions and criteria for the classification of crypto-assets as financial instruments, filed on 25 April 2024.

Contents

I. Templates for explanation and legal opinion – Standardized test (Draft guidelines)

Important considerations

ALFI's main advocacy points in this consultation are as follow:
ALFI, responding to this consultation from the perspective of investment funds part, within the buy-side of the industry, provided comments, proposed alignments and raised some concerns to be considered as the views of the investment fund industry, in a segment focused on cross-border distribution within the European Union and globally.

1. **Diverging interpretations across member states / regulatory uncertainty**: Given the local transpositions of MiFID across Europe and the reliance thereof, in the qualification of crypto-assets under MiCAR, it is important to avoid a legal opinion in one member state to unilaterally qualify as a crypto asset, an instrument that would have qualified as a financial instrument under the MiFID transposition in another member state.
2. **Single standard template**: Given the similarities between the two templates proposed in Annex A and B, ALFI would be of the view that both the explanation and the legal opinion could be documented, using the same template, to avoid unnecessary complexity.
3. **Considerations for hybrid instruments**: ALFI welcome the approach by ESMA for the classification of hybrid tokens, consisting in prioritizing their qualification as financial instruments under MiFID -- rather than only considering their multi-faceted nature – as soon as a hybrid token embeds features of financial instruments. To allow for particular care be given to hybrid instruments and their respective qualification, both the template and the standardised test should allow for specifically documenting the characteristics of hybrid instrument, and the resulting qualification.

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Response to consultation

Question 1 – Do respondents have any comments on the template for the purposes of Article 8(4) Regulation (EU) 2023/1114?

General considerations:
Diverging interpretations across member states / regulatory uncertainty: ALFI welcome the approach by ESMA for the classification of hybrid tokens, consisting in prioritizing their qualification as financial instruments under MiFID -- rather than only considering their multi-faceted nature – as soon as a hybrid token embeds features of financial instruments. In this regard, we would highlight the concern that, the definition of financial instruments being based on the MiFID Directive, the qualification criteria may slightly diverge among member states. To this respect, the exclusion of financial instruments, being a criterion for the definition of crypto-assets under the MiCA Regulation, may consequently differ across jurisdictions, notwithstanding a uniform application of the regulation across the board. We would raise concerns about the

subsequent regulatory uncertainty, should issuers of crypto asset be tempted to select the legal advisor to provide the legal opinion for the qualification of the crypto asset, based on the suitability of the local transposition of MiFID. Eventually, such legal opinion would be valid across Europe, leading to inconsistencies in some jurisdictions where the same instruments would have qualified as a financial instrument under MiFID.
Beyond the template, it is important to avoid a legal opinion in one member state to unilaterally qualify as a crypto asset, an instrument that would have qualified as a financial instrument under MiFID transposition in another member state.

Single standard template: ALFI considers that, for the main part, the two annexes A and B are similar. In order to avoid unnecessary complexity, we would be of the view that both the explanation and the legal opinion could be documented, using the same template. In this unique template, any specific fields limited to the context of asset reference tokens could be identified as such, to avoid any confusion.

Hybrid instruments: in line with our response to the ESMA consultation on the Third batch of policy mandates under MiCAR, dated 25 April 2024, we reiterate that particular care should be given to hybrid instruments of payment and their respective qualification. Hybrid instruments would result particularly sensitive to potentially diverging interpretations, at local countries level, with regards to their qualification as instruments of payments. We would advise that both the template and the standardised test should allow for specifically documenting the characteristics of hybrid instrument, and the resulting qualification.

Specific to Q1:

As mentioned in the above general considerations, considering the extensive similarity between the two templates proposed, for documenting the qualification of crypto assets other than EMT and ART, and of ART respectively, we would be of the view that providing two separate templates would lead to unnecessary complexity. We would suggest that combining the both into one single template, while customising some specific fields to the needs of ART, would serve the requirement for completeness of information while reducing the complexity.
Similarly, specific consideration should be given to the case of hybrid instruments: we would advise adding, in the template, a specific line concerning justification on the analysis of hybrid instrument and documentation of the corresponding characteristics.
In the same vein, we would be in favour of a clarification with regard to the applicable regime and corresponding justification to bring into the explanation / opinion documentation for stablecoins, so as to avoid any misuse of regulatory interpretation or similar arbitrage towards the most favourable local regime. In particular, such clarification should address the notion of instrument of payment, for such notion is closely linked to the subsequent qualification of financial instruments under MiFID.

Question 2 – Do respondents have any comments on the template for the purposes of Article 17(1) point (b)(ii) and Article 18(2) point (e) of Regulation (EU) 2023/1114?

With regard to classification of instruments and the respective qualification, ALFI is of the view that there is merit in keeping the existing local flexibility, currently existing with regards to the qualification as financial instruments. We see some regulatory uncertainty, derived from MiFID being a Directive subject to local transpositions on the one hand, and the MiCA Regulation being directly applicable by all member states on the other hand.
While MiCA is a regulation that is directly applicable by all member states, the qualification of financial Instrument under MiFID is subject to interpretation, following the transposition at local level.
In line with this consideration, should an instrument qualify as a crypto asset under MiCAR, based on a legal opinion issued in one-member country, then such legal opinion would classify the instrument as a crypto asset in all member states, and therefore, de facto, disqualify from a financial instrument in all markets across the Union. Yet, should that instrument be assessed in another member state, it may have qualified as a financial instrument under MiFID, as per the local transposition. This would have a substantial impact on the eligibility of such instrument for investment by investment funds domiciliated in member states of the Union, and in particular in those member states, such as Luxembourg, that do not allow certain categories of investment funds open to retail investment, such as UCITS, to invest in crypto assets under MiCAR.
Under such considerations, we would advise that these guidelines under MiCAR would be implemented in line with the approach to qualification of instruments already in place with MiFID, so as to avoid issuers of crypto assets to find arbitrage opportunity across the different countries in the Union, based on their expected target market for the instrument issued, seeking a legal opinion in one or the other specific jurisdiction, to qualify as a crypto asset, to the detriment of the industry and the final investors overall.
Similarly, as explained in our response to Q1, we would be in favour of clarification with regards to the applicable regime for stablecoins, and instruments of payments in general, as it constitutes a decisive element in the qualification of financial instruments under MiFID.

In all instances, and while there may be different interpretations, in different countries, with regards to the qualification of financial Instrument under MiFID, we would strongly remain in favour of a qualification approach that would follow the principle of substance over form.
Reiterating our consideration from our response to the previous consultation on the qualification of financial instruments, a financial instrument exchanged via a DLT or similar technology remains a financial instrument under MiFID.
In the interest of a streamlined implementation of the different pieces of regulation across the Union, as well as to avoid any regulatory uncertainty among member states, we would advocate for qualification processes that offer the same flexibility and similar principles, with regards to the qualification of crypto assets, as currently implemented for the qualification of financial instruments under MiFID. We would consider that a simplified template, in particular with regards to the lists of exceptions, would serve this purpose.

Question 3 – Do you consider that the fields of the template relating to explanations as to regulatory status are sufficiently clear and would enable a proportionate completion in line with

the simplicity or complexity of the structure of the crypto-asset to which the explanation or legal opinion relates?

As described in our response to Q.2, we would be in favour of a simplified template, in particular with regards to the lists of exceptions.
We understand the list of exception is reflecting the exceptions as described in the Level 1 Regulation. Yet, we are of the view that the below list of exceptions gathers an heterogenous series of elements, such as products, but also instruments, as well as some specific investment vehicles related to targeted pieces of regulation (e.g. social pension schemes). Such absence of uniformity in the nature of the elements in the exclusion list may generate legal uncertainty, with particular consideration to the local rules applied to specific investment vehicles.
"Opinion, with detailed explanation, that the crypto-asset to which this opinion relates is not any of:
- Financial instrument
- Deposits
- Funds
- Securitisation positions
- Non-life or life insurance products or reinsurance or retrocession contracts
- Pension product
- Officially recognised occupational pension schemes
- Individual pension products
- Pan-European Pension Products
- Social security schemes"
Would it be appropriate to consider presenting a simplified list of exceptions, while remaining in compliance with the Level 1 Regulation? Such a simplification could consist on the demonstration that the instrument would qualify as a crypto asset, on the substance elements differentiating from financial instruments under MiFID in particular. Such principle-based demonstration would therefore follow the underlying essence of MiFID, focusing on the interest of the investors and following a risk-based approach, rather than proposing a mere tick-the-box exercise.

This being said, we would like to raise concerns that, beyond the initial asset-classification task, some criteria seem to having been omitted in the template. More specifically, we would consider that the notion of "significant crypto asset", some elements from art 40 under MiCA and prohibition to granting interest, are missing and would see merit in being included in the template for explanation and opinion as elements in the qualification of crypto assets. Such justifications could be either presented in the last field of the template, i.e. in the opinion "that the crypto-asset is within the meaning of Article 3(1), point (6) MiCAR", or it could be presented in a separate field.

Question 4 – Do respondents have any comments on the standardised test?

As a general consideration, we welcome the approach by ESMA for the classification of hybrid tokens, consisting in prioritizing their qualification as financial instruments under MiFID -- rather

than only considering their multi-faceted nature – as soon as a hybrid token embeds features of financial instruments (list of such features could be confirmed in the Technical Standards). Such general approach would avoid further fragmentation of opinions, with regards to the same hybrid assets, in different jurisdictions across the EU.

With regards to the specific elements of the test referring to Art 2(3), aiming at defining if the crypto-asset is unique and not fungible with other crypto-assets, we would like to reiterate the concerns, raised in the ALFI's response to the ESMA consultation on the Third batch of policy mandates under MiCAR, dated 25 April 2024 and related to the qualification of crypto assets as financial instruments:
Particular consideration should be given, when considering the definition of "instruments of payment". While we agree that the definition of "instruments of payments" allows for crypto-currencies to be clearly defined out of the scope of instruments qualifying as financial instruments, particular care should be given to hybrid instruments of payments and their respective qualification.
In particular, we would like to raise concern as to potentially diverging interpretations, at local countries level, with regards to qualifications as instruments of payments. Further clarification would be needed regarding the payment function of a crypto-asset that may cumulate both a potential payment function and an investment purpose. We would appreciate specific clarification around the notion of instrument of payment in the context of PSD/PSR to foster a consistent assessment where it relates to "other crypto-assets" such as bitcoin. To this respect, we would advise to provide further clarity in the definition.
With regards to the criteria and conditions proposed for hybrid-type tokens, we consider that the quote "features of financial instruments" suggests some uncertainty and could lead to various interpretations. This term of "features" is considered as too vague and would benefit from further clarifications. In all instances, clarification would be appreciated in defining whether the ESMA intends to support the position that the hierarchical approach should be adopted once all characteristics of a financial instrument are satisfied, or alternatively when the instrument under consideration presents certain minimum characteristics.
Such clarification could take the form of a series of examples in the guidelines.

In addition, we would like to raise concerns on the fact that:

i) All crypto-assets could have hybrid features and require specific consideration and clarification, as described above
ii) Crypto assets features could evolve over time. Resultingly, uncertainty could arise from the fact that features at time of issuance could evolve throughout the life of the instrument, and its qualification as a financial instrument could therefore vary over time. To this respect, guidance should be given as to whether the qualification as a financial instrument is that of issuance day, or should be reassessed over time. To this respect, some flexibility could be allowed with respect to the form such reassessment could take.

Based on the precedence of the qualification of the asset as a financial instrument, and considering the potential dynamic nature of the features of crypto assets through time (to anticipate on financial innovation), one should not omit the possibility of reclassification of such instrument. We consider that such reassessment or reclassification at a later stage would be in the best interest of investors, to foster clarity and transparency on the characteristics of their

investments. We would appreciate clarification and principle-based guidance to this regard, following a pragmatic approach and in consideration of the principle of proportionality. Such clarification could include details on how to subsequently use the template initially completed, to document this reassessment.

Moreover, we would advise addressing, in the standardized test, specific consideration for the qualification of hybrid instruments, below the list of exclusions under Art 2(4). This could take the form of a specific question or test inserted, on whether the instrument is a hybrid instrument of payment or a crypto currency.

Eventually, and with regards to suggestions aiming at simplifying and streamlining the test elements, and the list of exceptions in particular, we would refer to our response to Q3.

About ALFI

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Created in 1988, the Association today represents over 1,500 Luxembourg domiciled investment funds, asset management companies and a wide range of business that serve the sector. These include depositary banks, fund administrators, transfer agents, distributors, legal firms, consultants, tax advisory firms, auditors and accountants, specialised IT and communication companies. Luxembourg is the largest fund domicile in Europe and a worldwide leader in cross-border distribution of funds. Luxembourg domiciled investment funds are distributed in more than 70 countries around the world.