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MiCAR: ESMA consults on draft guidelines on reverse solicitation exemption for third-country firms

The European Securities and Markets Authority (ESMA) published a consultation paper on draft guidelines on the reverse solicitation exemption for third-country firms under the Markets in Crypto-Assets Regulation (MiCAR) at the end of January 2024.

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Background

Under Article 59 of MiCAR, entities will require an authorisation to provide crypto-asset services within the EU unless an exemption applies. Article 61(1) of MiCAR contains a reverse solicitation exemption for third-country firms whereby, in circumstances where a client (including a prospective client) established or situated in the EU initiates at its own exclusive initiative the provision of a crypto-asset service or activity by a third‑country firm, the requirement to be authorised as a crypto-asset service provider (**CASP**) under MiCAR will not apply to the provision of that crypto-asset service or activity by the third-country firm to that particular client.

The exemption will not apply in circumstances where a third-country firm markets new types of crypto-assets or new crypto-asset services to a client that has requested the provision of a crypto-asset or crypto-asset service at its own exclusive initiative.

The stated rationale for the exemption is that clients should not be excluded from using third-country firms if they choose to do so without having been solicited by such firms.

As expected, the requirements in MiCAR regarding reverse solicitation are restrictive. Third-country entities seeking to access EU customers or investors should make themselves aware of the restrictions. In our view, reverse solicitation cannot be an underlying strategy if there is to be regular accessing of EU customers/investors. Therefore, the application of the reverse solicitation exemption, like in other spheres of financial services, should be done on a case-by-case exercise.

Draft guidelines

Article 61(3) of MiCAR mandates ESMA to issue guidelines that provide more clarity to national competent authorities (**NCAs**) and market participants on the limited situations where the offer or provision of crypto-asset services to clients established or situated in the EU would be regarded as initiated at the own exclusive initiative of a client by:

- specifying the situations in which a third-country firm is deemed to solicit clients established or situated in the EU
- recommending supervisory practices that NCAs may take to detect and prevent the circumvention of the reverse solicitation exemption

ESMA issued the draft guidelines to seek stakeholder input on the proposed content before finalising the document. The consultation closed on 29 April 2024.

Factors to consider when determining when a third-country firm solicits clients established or situated in the EU

Means of solicitation

The term solicitation should be construed in the widest possible way and in a technology neutral way. The draft guidelines specify that it includes the promotion, advertisement or offer of crypto-asset services or activities to clients in the EU by any means, including by way of and without limitation:

- offers of a general nature and addressed to the public
- internet commercials
- brochures, telephone calls
- face-to-face meetings
- press releases
- brand advertisements by way of sponsorship deals
- any other form of physical or electronic means, including social media platforms and mobile applications (among others)

ESMA states in the consultation paper that due to the broad interpretation of the term, solicitation includes banner advertisements and solicitation by any kind of affiliates, such as influencers or other celebrities, reflecting the fact that crypto-assets and crypto-asset services are essentially offered online.

Location of clients

To assess whether a third-country firm solicits clients established or located in the EU, all facts and circumstances of the case are relevant. For example, a website in an official language of the EU (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 EU.

In contrast, geo-blocking to prohibit access to a website by clients established or located in the EU would be a strong indication that a third-country firm is not soliciting clients in the EU via such website.

Person soliciting

The draft guidelines prescribe that solicitation may occur irrespective of the person through whom it is performed. The solicitation may be carried out either by the third-country firm itself or by any other person acting explicitly or implicitly on behalf of the third-country firm or having close links to it (as defined in MiCAR). The draft guidelines provide examples of instances where a person may be acting on behalf of a third-country firm.

Furthermore, ESMA states in the consultation paper that the relationship between the third-country firm and the person soliciting on its behalf does not necessarily need to be a contractual relationship. For example, if a third party undertakes a marketing campaign or takes action to build the third-country firm's profile in the EU, the third-country firm would not be able to claim that there was no solicitation, and the reverse solicitation exemption would not apply.

Importantly, solicitation done on behalf of a third-country firm by a person or entity regulated in the EU should be regarded as a breach of MiCAR irrespective of whether the third-country firm is part of the same group or not. Therefore, solicitation by a third-country firm through re-direction of clients via a regulated group entity's website would fall foul of the exemption.

Exclusive initiative of the client

A firm should not be deemed to solicit clients if the crypto-asset service or activity is provided at the own exclusive initiative of the client. The draft guidelines specify that the client's own exclusive initiative should be construed very narrowly and the assessment as to whether or not contact was exclusively initiated by the client should be a factual one. Contractual arrangements or disclaimers cannot supersede contrary facts.

The time of the request from the client or of the offering, promotion or advertisement is critical to an assessment. If a third-country firm meets all the conditions to rely on the reverse solicitation exemption, it may only do so for a very short period of time. A third-country firm relying on the exemption is not allowed to subsequently offer a client further crypto-assets or services, even if such crypto-asset or service is of the same type as the one originally requested, unless they are offered in the context of the original transaction. Although the daft guidelines do not provide a definite time period during which the exemption may be relied upon, the draft guidelines indicate that the lapse of one month (or even a couple of weeks) between the provision of the crypto-asset service based on a request made at the own exclusive initiative of the client and a subsequent offer by the third-country firm could exclude the application of the exemption.

The draft guidelines also state that third-country firms should be able to provide records that track the relationship with the client and whether the client has taken the initiative to receive crypto-asset services with respect to a new product.

When is a crypto-asset or crypto-asset service of the same type as another one?

As noted above, the reverse solicitation exemption will not entitle a third-country firm to market new types of crypto-assets or crypto-asset services to a client that has requested the provision of a crypto-asset or crypto-asset service at its own exclusive initiative. The draft guidelines state that this leaves open the possibility for a third-country firm to market or offer crypto-assets or crypto-asset services of the same type as the one originally requested by the client, subject to satisfying the criteria in the draft guidelines.

The draft guidelines provide guidance on how to assess whether a crypto-asset or crypto-asset service is of the same type as another. The draft guidelines provide that such assessment should be made on a case-by-case basis, taking into account elements such as the type of crypto-asset or crypto-asset service or activity offered and the risks attached thereto.

The draft guidelines set out the following non-exhaustive examples of pairs of crypto-assets that would not be considered as belonging to the same type of crypto-assets:

- utility tokens, asset-referenced tokens or e-money tokens
- crypto-assets not stored or transferred using the same technology
- e-money tokens not referencing the same official currency
- asset-referenced tokens based mostly on FIAT currencies and asset-referenced tokens having significant crypto-currency ponderations
- liquid and illiquid crypto-assets
- crypto-assets other than asset-reference tokens and e-money tokens with a non-identifiable offeror and crypto-assets other than asset-reference tokens and e-money tokens with an identifiable offeror

ESMA also provides additional commentary regarding when a crypto-asset or crypto-asset service is/is not of the same type as another.

Supervisory practices to detect and prevent circumvention of the reverse solicitation exemption

With respect to supervisory practices, the draft guidelines highlight the following actions that NCAs can take to detect significant EU-based activity by third-country firms:

- monitoring of marketing activities targeting EU based clients via:
    - searches for third-country firms with telephone numbers starting with EU local country codes or email or website addresses indicating their presence, at least virtual, in the EU (e.g. URL or email address ending with ‘lu’, ‘de’, ‘fr’, etc.)
    - marketing monitoring tools, especially those with the ability to monitor social media activity as they may indicate the geographic markets targeted by third-country firms
- conducting consumer surveys to identify the firms used by clients in an EU jurisdiction for crypto-asset services
- cooperating with other NCAs and other authorities that might have insight into whether third-country firms are offering services in an EU jurisdiction such as the police and local tax authorities
- following-up on complaints from clients or information from whistleblowers indicating that a third-country firm might have been soliciting clients in an EU jurisdiction

Comparison to the MiFID II framework

Article 42 of MiFID II contains a similar reverse solicitation exemption in respect of the provision of investment services and activities in the EU. Article 42 was transposed into Irish law by Regulation 51 of the European Union (Markets in Financial Instruments) Regulations 2017 (**MiFID Regulations**).

Regulation 51 of the MiFID Regulations provides that where a retail or professional client established or situated in the EU initiates, at its own exclusive initiative, the provision of an investment service or the performance of an investment activity by a third-country firm, the requirement for authorisation as an investment firm under the MiFID Regulations will not apply to the provision of that service or the performance of that activity by the third-country firm to that person. A client’s own exclusive initiative will not entitle the third-country firm to market (other than through a branch) new categories of investment products or services to that client.

As such, the reverse solicitation exemption under MiCAR tracks the wording of the reverse solicitation exemption under the MiFID Regulations/MiFID II subject to the absence of reference to a branch of a CASP.

In relation to the draft guidelines, the provisions mainly follow the established practice under the MiFID II framework as prescribed by ESMA Q&As, but not in all respects, i.e. the guidance for assessing if an investment product or service is a new category of product/service or not differs to the guidance for assessing if a crypto-asset or crypto-asset service is a new category or not.

Next steps

The consultation on the draft guidelines closed on 29 of April 2024.The final report is expected to be published in Q4 2024.

MiCAR will apply from 30 December 2024, with the exception of Titles III and IV of the Regulation (which address the frameworks for asset-referenced tokens and e-money tokens) which have applied since 30 June 2024.

For further information on this topic, please contact Patrick Brandt, Partner, Ciara Brady, Senior Associate, Louise Hogan, Senior Associate, Sarah Lee, Senior Knowledge Lawyer or any member of ALG's Financial Regulation Advisory team.

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