

RESPONSE TO CONSULTATIONS

MARKET IN CRYPTO ASSET

RTS and guidelines with regards detecting and reporting suspected market abuse, suitability requirements, transfers of crypto assets and digital resilience, in the context of MiCA

Luxembourg, 24 June 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 Securities Market Authorities (ESMA) for the opportunity to participate in this second part consultation on the third batch of policy products of MiCA.

Our members appreciate the opportunity to share the views of the market practitioners in Luxembourg, with regards to detecting and reporting suspected market abuse, suitability requirements, transfers of crypto assets and digital resilience, in the context of MiCA.

In order to provide evidence of the industry considerations with regards to those various topics in the context of MiCA, answers will be given on a number of selected questions focusing on priorities stemming from industry-related consideration and impact assessment.

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I. Arrangements, systems and procedures for detecting and reporting suspected market abuse in crypto assets (Draft RTS)

Important considerations

(This part is to be used by ALFI Communications Dept in the accompanying press release)

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. **Scope:** While agreeing with ESMA's analysis on the personal scope of Article 92 of MiCA, ALFI considers that, due to their respective roles and responsibilities within the investment management value chain, depositaries should not be considered as PPAETs.
2. **Roles and responsibilities:** while IFM are included in the scope of the MAR and comply with the regulation thereof, concerns are raised with regards to their inclusion in the scope of the proposed new regime under MiCA. Specifically, the role of the AIFM should be limited to performing due diligence on the Portfolio Manager to ensure that they do have the arrangements, systems, procedures to report STOR, and that they duly report the STORs accordingly.
3. **STOR template:** In the interest of cost efficiency, we would consider important to build on the existing STOR template, while keeping the adjustment to the minimum fields specific to transactions on crypto assets via a blockchain. Since concrete background information and cases are still limited, ALFI advise the template should be reviewed at a later stage, following a risk-based approach, building on previous cases of STOR reporting.

Response to consultation

Question 1 – Do you agree with ESMA's analysis on the personal scope of Article 92 of MiCA? Are there other types of entities in the crypto-asset markets that should be considered as a PPAET (e.g. miners/validators)? Do you believe that CASPs providing custody and administration of crypto-assets on behalf of clients should also be considered as PPAETs for the purpose of this RTS? Please elaborate.

General considerations:

While the industry respondents may be representing various standpoints, depending on their relative roles, responsibilities and positioning in the value chain of finance and asset management, we would like to highlight the consideration that we are responding from the perspective of investment funds part, within the buy-side of the industry. The comments provided, the alignments we propose and the concerns we raise are 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.

Specific to Q1:

Overall, we agree with ESMA's analysis on the personal scope of Article 92 of MiCA.

Nevertheless, considering the various actors and their respective roles and responsibilities within the investment management value chain, we are of the view that entities providing safekeeping and administration of crypto assets (in particular, depositaries and custodians) should not be considered as part of the transaction chain within the meaning of article 16(2) of the Market Abuse Regulation EU 596/2014 (MAR). Hence these entities should not be considered as PPAETs.

Question 2 – Do you agree with the proposed elements that should constitute appropriate arrangements, systems and procedures to detect and prevent market abuse? If not, please specify the article of the draft RTS and elaborate.

From a general standpoint, ALFI agree with the proposed elements, considering that they are in line with the provisions of article 16(2) MAR, as well as the guidance provided by ESMA 2015 Report on MAR.

From a more granular standpoint, we base our consideration on the local supervisory assessments. In 2022, the Luxembourg Commission de Surveillance du Secteur Financier (CSSF) launched a thematic review on the STOR obligations of Investment Fund Managers (IFMs) under Article 16(2) MAR. The review is part of the measures taken by the CSSF following the findings made in 2019 in the ESMA Peer Review on STORs.

On 25 January 2023, the CSSF published its report of general findings and observations as regard the 2022 Thematic Review on STOR Obligations of Investment Fund Managers (IFMs). The feedback suggests that in many cases, most of the applicable technical standards were fulfilled by the market participants.

Against this background, considering that IFMs are already under the scope of MAR and complying with this Regulation, we are not sure that IFMs are the typical type of entities that should be specifically targeted by the new regime.

Moreover, we would like to emphasise the fact that most AIFM do, in their operating model, delegate the portfolio management function. In practice, AIFMs do not have a trading desk internally, nor do they execute trades.

Should the Portfolio Manager (PM) be located in the EU, they should be subject to the Market Abuse Regulation and the role of the AIFM should be limited to performing due diligence on the PM to ensure that they do have the arrangements, systems, procedures to report STOR, and that they duly report the STORs accordingly. Following a risk-based approach, the controls performed by the AIFM should be limited to the periodic due diligence review on the portfolio manager to this regard.

This being said, we agree that the AIFM retains the responsibility to perform an initial due diligence and an on-going monitoring on the delegated portfolio manager, notably to ensure that the PM does have the arrangements, systems, procedures to report the suspicious transaction and order reports (STOR).

Should the PM be located outside the EU, the AIFM shall ensure the PM does have similar regulatory requirements as those in the EU and consequently similar arrangements, systems and procedures with regards to STOR.

Question 3 – Do you agree with the proposed STOR template as presented in the Annex (p.51-56) of the RTS?

The [current template](https://www.cssf.lu/en/Document/form-to-be-used-to-notify-suspicious-transaction-and-orders-reports-stors/) applicable in our jurisdiction (<https://www.cssf.lu/en/Document/form-to-be-used-to-notify-suspicious-transaction-and-orders-reports-stors/>) already covers many of the expected notions.

Minor adjustments could be envisaged without fully revamping or replacing the current MAR form.

ALFI take the view that the current template is appropriate and we propose the following minor adjustments to make the template fit-for-purpose for transactions on crypto-assets via a DLT:

- Identification of the blockchain the transaction was performed on, and mention of the distinction private / public blockchain
- The LEI (Legal entity identifier) of the reporting entity of the transaction
- The unique identifier of the transactions on the blockchain
- The "Relevant fields for description of the crypto asset" are mentioned in the corresponding field.

In the interest of cost efficiency, we would consider important to build on the existing STOR template, while keeping the adjustment to the minimum fields mentioned above.

Question 4 – Is there any parameter or naming convention that in your view should be modified to facilitate the identification of suspicious orders/transactions/behaviours involving crypto-assets?

At this stage, ALFI do not have particular views as regards the parameters and naming conventions that would be more adequate to identify suspicious orders, transactions or the functioning of the distributed ledger technology.

Question 5 – In Section II of the Annex, would the concept of 'location' be applicable to a distributed ledger? For instance, would the IP address of miners/validator nodes in the network be useful in a context where it can be masked through VPNs?

At this stage, in absence of specific legal grounds, we would not have any strong views on the relevance of the concept of location, to identify a decentralised infrastructure.

Question 6 – Is there any other element or information relevant to crypto-asset markets that in your view should be included in the template? Please explain.

At this stage, and echoing our response to Q3 with regards to cost efficiency in the implementation of the present technical standards by the market participants, we would not propose any additional element that should be included in the current template.

Considering the current lack of background information on STOR reporting with regards to transactions on crypto assets performed on a DLT, we would be of the view that a reassessment of the STOR template should be considered at a later stage, to benefit from the market experience. The design of the template should be reviewed following a risk-based approach, building on previous cases of STOR reporting, and considering any missing field in such reports, from practitioners' standpoint.

Question 7 – Please provide information about the estimated costs and benefits of the proposed technical standard, in particular in relation to the arrangements, systems and procedures to prevent and detect market abuse.

As regards to the location of players outside the EU (including decentralised infrastructures), we are of the view that the current framework provided by the [Commission Delegated Regulation \(EU\) 2021/1783](#) supplementing Regulation (EU) No 596/2014 (MAR) in relation to cooperation arrangements with third countries should be developed further.

Following the approach already in place for traditional financial instruments, should the Man Co delegate the portfolio management, the reporting should be performed by the delegated PM to its local National Competent Authority (NCA) in the Union, and the local NCA should communicate adequately to the respective local NCA of the Management company.

In line with such considerations we would not see any incentive in changing this current practice, as we consider this practice of communication, as currently in place among NCAs, is appropriate and effective.

II. Suitability requirements applicable to portfolio management in crypto-assets and format of periodic statement (Guidelines)

Important considerations

(This part is to be used by ALFI Communications Dept in the accompanying press release)

ALFI's main advocacy points in this consultation are as follow:

1. **Investors' protection:** ALFI emphasise the purpose of the suitability assessment, being to ensure investors' protection and to avoid unsuitable investment advice on crypto assets, hence is in favour of the CASP applying similar suitability assessment as applied under MiFID II.
2. **Consistency MiCA / MiFID II:** fostering the convergence of both pieces of regulation is appropriate to ensure a level playing field between the transactions on traditional financial instruments and the transactions on crypto assets, under the *same activity, same risk, same regulatory outcome* principle
3. **Clear, complete and available information:** the white paper should be as detailed, clear, complete as necessary, for both the CASP and the client to transacting, have a complete, clear and unambiguous understanding of the risk profile and purpose of the crypto asset considered in the transaction. Furthermore, periodic statements should allow for a "push" publication to the client, in complement to posting on a portal.

Response to consultation

Question 8 – Do you agree with ESMA's approach regarding consistency between the MiCA and MiFID II suitability regimes? If you think that the two regimes should diverge, where and for which reasons?

As a preliminary consideration, we would like to reiterate the purpose of the suitability assessment, being to ensure investors' protection and to avoid unsuitable investment advice on crypto assets.

From a general standpoint, ALFI is in favour of the CASP applying similar suitability assessment as applied under MiFID II.

While we understand the additional burden and administrative work involved in performing such suitability assessment are not to be understated, we are of the view such suitability requirement analysis would meet the requirements with regards to investors' protection.

Furthermore, we would consider such conversion between MiCA and MIFID II would be appropriate in ensuring a level playing field between the transactions on traditional financial instruments and the transactions on crypto assets, under the *same activity, same risk, same regulatory outcome* principle.

Question 9 – Do you think that the draft guidelines should be amended to better fit crypto-assets and the relevant crypto-asset services? In which regard? Please justify your answer.

As stated in our response to Q8, ALFI is of the view that the proposed guidelines appropriately converge with the requirements of MiFID II and we are in favour of this approach. In the particular case of crypto asset transactions, we would be in favour of further highlighting the requirement for the white paper of the crypto asset to be as detailed, clear, complete as necessary, to ensure both the CASP and the client (or prospective client) would, prior to transacting, have a complete, clear and unambiguous view of the risk profile and the purpose of the crypto asset considered in the transaction.

Question 10 - Do you agree with the approach followed by ESMA regarding periodic statements provided in relation to portfolio management of crypto-assets?

ALFI agree that the periodic statement and the proposed guidelines are aligned with the standard practices to this regard and the electronic media is adequate in the context of crypto asset.

This being said, and in the interest of efficiency in serving the underlying requirement of investors' protection and completeness of information at their disposal, we would advise that the CASP should have the possibility to "push" the periodic report to the client, rather than only making such report available on a portal. Such "push" process could be optional and triggered by the client requirement, in a parameterizable way for each respective client or prospective client.

III. Procedures & policies, in the context of transfer services for cryptoassets (Guidelines)

Important considerations

(This part is to be used by ALFI Communications Dept in the accompanying press release)

ALFI's main advocacy points in this consultation are as follow:

1. **Alignment among NCAs:** in the best interest of market participants active in cross-border distributions, convergence between NCAs would be appreciated in all aspects, including interpretation of the Regulation, definitions, methodology and oversight practices to ensure a level playing field across the Union
2. **Risk reassessment:** ALFI reiterate the consideration that all investments in crypto assets bear substantial risks for the investors. As the industry may be lacking background substantiated usecases. We suggest the guidelines may benefit from being revised at a later stage to ensure the different risks are properly, adequately and proportionally addressed.

Response to consultation

Question 11 – Do you agree with the approach taken by ESMA in the draft guidelines for crypto-asset service providers providing transfer services for crypto-assets on behalf of clients as regards procedures and policies, including the rights of clients? Please also state the reasons for your answer.

While we agree the proposed guidelines are appropriate and compliant with the standard processes, for transfers within the EU, we would require some additional consideration with regards to transfers to or from a third country outside the Union.

From a practitioner standpoint, we understand that in the meaning of these guidelines, the service providers providing transfer services for crypto assets are the CASPs.

To this regard, and referring to the point 4.2 (10.) of the guidelines, we would appreciate clarifications as regards to the absence of a requirement for the crypto asset service providers to demonstrate their effective compliance with these guidelines. Clarification would be appreciated, regarding to the individual power of the NCA to require, locally, specific reporting on the respective compliance of the CASPs locally.

Irrespective of such national requirements and in the best interest of market participants active in cross-border distributions, in particular considering the cross-border scope of transactions on crypto-assets, we would like to emphasise that convergence between NCAs would be appreciated, in all aspects. Such aspects include, but are not limited to interpretation of the Regulation, definitions, methodology and oversight practices with regards to the guidelines by the respective NCAs.

Such convergence requirement among the NCAs is aligned with the overarching principles fostered by the ESMA, with views to ensure a level playing field across the Union.

Question 12 – Do you think that the draft guidelines address sufficiently the risks for clients related to on- and off-DLT crypto-asset transfers? Please justify your answer.

In addressing this question, we would like to reiterate the consideration that all investments in crypto assets bear substantial risks for the investors. The respective consideration that there would be “no such thing as a safe investment in crypto asset” was highlighted in the first consultation paper in this pack RTS, to which ALFI provided a targeted response in April 2024. To this regard, ALFI would consider that the industry may be lacking background substantiated information on the topic. We would therefore suggest that the guidelines may benefit from being revised at a later stage to ensure the different risks are properly, adequately and proportionally addressed across the board.

Question 13 - Are there any additional comments that you would like to raise and/or information that you would like to provide, for example, on whether other relevant points or clients' rights should be considered?

ALFI do not have any particular consideration to this regard.

IV. Maintenance of systems and security access protocols (Guidelines)

Important considerations

(This part is to be used by ALFI Communications Dept in the accompanying press release)

ALFI's main advocacy points in this consultation are as follow:

1. **ICT and connectivity systems:** in the context of crypto assets, ALFI consider both ICT systems and connectivity systems, providing statements from distant CASP or distant service providers to the depositary, should be included in the scope of the guidelines.
2. **Due diligence:** ALFI advise adequate requirement be put on the distant CASP and service providers to comply with any due diligence requirements initiated from the depositary and the AIFM, within the scope of their respective oversight duties.
3. **TIBER-EU framework:** ALFI consider the TIBER-EU framework can be a relevant EU framework, as a standard for this mandate.
4. **Proportionality principle:** In all instances, ALFI is in favour of applying the proportionality principle in the guidelines with the inclusion of minimal administrative arrangements, while fostering operational flexibility in the implementation.

Response to consultation

Question 14 – Do you support ESMA's interpretation of the term, 'systems' in the mandate? If not, please explain your understanding of the term (and provide examples if possible).

From a general standpoint, and as applied to the context of crypto assets, ALFI would agree with the interpretation of the ESMA of the term "systems", considered as ICT systems.

Yet, we are of the view that connectivity systems, providing statements from distant CASP or distant service providers to the depositary, should not be overlooked in the scope of the present guidelines.

To this regard, we would emphasize the requirement, for the distant CASP or distant service providers to comply with any due diligence requirements initiated from the depositary, within the scope of their respective oversight duties. Same considerations apply to the AIFM oversight and due diligence requirements.

Question 15 – Are there other 'appropriate Union standards' beyond those identified in the consultation paper that you consider relevant for this mandate? If yes, please list them and provide a rationale for why they would be relevant.

ALFI consider the TIBER-EU framework can be a relevant EU framework for this mandate (to the extent that the TIBER-EU framework does not contradict the new DORA requirements) since this framework aims to

- (i) test the resilience of financial market entities,
- (ii) facilitate the testing of cross-border entities subject to the supervision of several authorities and
- (iii) help entities to better understand their capabilities in terms of protection, detection and response, and to fight against cyber-attacks.

The CSSF and Central Bank of Luxembourg have jointly adopted this framework.

Question 16 - Do you agree with the inclusion of minimal administrative arrangements in Guideline 2 (i.e., no reference to implementing a risk management framework)? If no, please explain whether you would consider either fewer or more administrative arrangements appropriate.

ALFI would agree with the inclusion of minimal administrative arrangements in Guideline 2, considering that the proportionality principles overarchingly apply in MiCA. This being stated, it remains the responsibility of each CASP and IFM to decide, further to performing their own risk assessment, to apply a full risk management framework. We would be of the view such flexibility is appropriate in this context and in line with a risk-based approach.

Question 17 - Do you support the inclusion of Guideline 5 on 'cryptographic key management'? Do you consider cryptographic keys relevant as either a 'system' or a 'security access protocol'? Is this guideline fit for purpose (i.e., can cryptographic keys be 'replaced' as implied in paragraph 29)?

ALFI do not have strong views to this regard.

About ALFI

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