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By online submission

08 February 2024

Dear Sir/Madam

Re: EMA response to EBA's Consultation Paper on Draft RTS to further specify the liquidity requirements of the reserve of assets under Article 36(4) of Regulation (EU) 2023/1114

We welcome the opportunity to provide input on the EBA's Consultation Paper on Draft Regulatory Technical Standards to specify the minimum contents of the liquidity management policy and procedures.

The EMA represents payments, crypto-asset and FinTech firms, engaging in the provision of innovative payment services, including the issuance of e-money, stable coins (including e-money tokens as covered by the EU's MiCAR), open banking payment services, and crypto-asset-related services. A full list of our members is provided in the appendix to this document.

The EMA was established some 20 years ago and has a wealth of experience in regulatory policy relating to payments, electronic money and more recently crypto-assets.

We would be grateful for your consideration of our comments, which are set out below.

Yours faithfully,

Dr Thaer Sabri
Chief Executive Officer
Electronic Money Association

EMA responses

The ESAs face an enormous challenge of producing a complex, comprehensive and highly technical body of MiCAR level 2 regulatory instruments and related guidelines within a tight timeframe. We are grateful for the staggered consultation process launched several months ago, but remain concerned that each instrument, the interdependencies between, and the consistency across, these instruments cannot be given the required full and holistic consideration. We therefore urge the EBA to keep the instruments that are now being developed under review well beyond the consultation phase and to engage in a close ongoing dialogue with national competent authorities who will be implementing the instruments in their evolving supervisory practices. This ongoing dialogue would also have to include the crypto- asset industry to benefit from both the wealth of insight that industry efforts to comply with all aspects of this new rulebook will generate and direct, first line feedback the industry can offer on the still rapidly evolving crypto-asset markets. The objective would have to be not only to translate the rulebook into effective and EU-wide fully harmonised supervisory practices, but also to provide assistance for the analysis needed to inform the review and reform of the MiCAR level 1 text wherever needed.

We note that according to Article 140 the European Commission will have to present by 30 June 2025 a report to the European Parliament and the Council on the application of MiCAR accompanied as appropriate by a legislative proposal. EBA and ESMA will be consulted, and we urge the EBA to engage in a dialogue with the industry to help identify and shape necessary amendments as early as possible.

Regarding specifically the regulatory technical standards addressing different aspects of issuers' liquidity risk management and applicable to all or different subsets of issuers (depending upon their classification as significant or the discretionary application of related MiCAR requirements to non-significant issuers of ARTs or EMTs) we encourage the EBA to work together with the European Commission towards a consolidation of the different level 2 instruments. It would be most helpful to merge over time the instruments that are now being proposed into a consistent compendium covering in a fully consistent fashion all regulatory technical standards pertaining to liquidity risks and their management under MiCAR. Such a comprehensive and consistent compendium of technical standards would facilitate implementation and compliance by both competent authorities and issuers. Eventually that compendium may well include all RTS related to MiCAR prudential requirements as they apply to issuers of ARTs and EMTs.

That said, we welcome the opportunity to comment on this specific Consultation Paper on Draft Regulatory Technical Standards to further specify the liquidity requirements of the reserve of assets under Article 36(4) of Regulation (EU) 2023/1114 ("MiCAR", "CP" and "RTS"). We would be grateful if our following comments were considered for the finalisation of the RTS and stand ready for engaging in an ongoing dialogue with the EBA and national competent authorities which we believe is warranted well beyond the close of this consultation.

Before turning to the specific questions put forward in the CP and as set out in more detail in our response to the EBA CP on adjustments to own funds requirements (EBA Consultation Paper on Draft Regulatory Technical Standards to specify the procedure and timeframe to adjust its own funds requirements for issuers of significant asset-referenced tokens or of e-money tokens subject to the requirements set out in Article 45(5)) we cannot emphasise enough the **enormous** problems caused for significant issuers of EMTs by the doubling of the de minimis threshold for bank deposits from 30% to 60% as referred to in Article 45 (7) (b). The CP acknowledges that the classification as significant triggers the application of prudential requirements that result in an increase of issuers' credit and liquidity risks, a corresponding significant increase of interconnectedness with the financial system and, hence, in combination a major increase of financial stability risk posed by issuers. These are most unfortunate and surely entirely unintended consequences of the classification of issuers as significant, and run counter to the very objective of MiCAR: to contain financial stability risk.

Besides the major increase in issuers' interconnectedness with the financial system, the multi-faceted enormous cliff-edge effect issuers are facing will threaten their viability and sustainability. It offers them few – if any – options to rebuild a profitable business model that is capable of ensuring compliance with the full range of much increased prudential requirements, including the related internal governance and risk management and internal control requirements. Customers may well experience harmful interruption of services by issuers that are forced to terminate their business because, due to classification as significant, it is not viable any longer.

We urge the EBA to consider the issue jointly with the European Commission and develop an approach to the interpretation of the MiCAR level 1 text that allows for the disapplication of the increased de minimis threshold for bank deposits of issuers of EMTs.

We note in this regard that the EBA proposes an interpretation *against* the wording of the MiCAR level 1 text for the application of the reporting obligation under Article 22. The EBA in its consultation paper on the related draft RTS ("Consultation Paper on the Draft Regulatory Technical Standards on the methodology to estimate the number and value of transactions associated to uses of asset-referenced tokens as a means of exchange under Article 22(6) of Regulation (EU) No 2023/1114 (MiCAR) and of e-money tokens denominated in a currency that is not an official currency of a Member State pursuant to Article 58(3) of that Regulation") suggests interpreting the reference in Article 22 (1) (d) to "transactions … within a single currency area" such as to also include transactions across different currency areas. An interpretation that **is in no way covered by the wording of the MiCAR level 1 text.**

Compared to the proposed interpretation of Article 22 (i) (d) against its wording, which we find highly problematic (see detailed comments in our response to that other consultation paper) we see ample room for a teleological interpretation of the MiCAR level 1 text across the chain of references (from Article 58 (1) (b) to Article 45 (1) to (4) and from Article 45 (7) (b) back to Article 45 (3)) that would allow not to apply to issuers of EMTs the increased 60% de minimis threshold for bank deposits provided for in Article 45 (7) (b). It is clear that the EU-legislator's intention, when introducing the significantly more stringent regime for issuers classified as significant, was to contain the perceived higher financial stability risks posed by these issuers. As set out very clearly in the EBA's CP, the consequences of the application of the 60% de minimis threshold are not just unintended, but much worse, they run counter to the intention of the EU-legislator and generate the exact opposite of what it wanted to achieve, i.e. containing financial stability risks. A teleological interpretation taking into account the "effet utile" doctrine of the European Court of Justice ("ECJ") would have to come to the conclusion that the reference for issuers of EMTs in Article 58 (1) (a) to Article 45 (3), which as such is targeted at ARTs, was not intended to also entail the application to issuers of EMTs of the increased de minimis threshold provided for in Article 45 (7) (b) with the most adverse consequences set out in the EBA's CP. Article 58 (1) (a) does NOT refer to Article 45 (7). Article 45 (7) is primarily addressed to the EBA mandating it to develop RTS for application to the issuers of ARTs that are targeted by Article 45. Accordingly, Article 45 (7) (b) stipulating the increase of the de minimis threshold for bank deposits to 60% refers to "deposits in <u>each</u> official currency referenced" (our mark-up). Towards the end of the provision again reference is made to "…<u>each</u> official currency" (our mark-up). ARTs, according to the definition in Article 3 (1) (6) can reference "another value or right or a combination thereof, including <u>one or more</u> official currencies" (our mark-up). EMTs cannot. An EMT is defined in Article 3 (1) (7) as "crypto-asset that purports to maintain a stable value by referencing the value of <u>one</u> official currency" (our mark-up). Thus, the wording of Article 45 (7) (b) clearly indicates that the EBA when developing the RTS is bound by the increase of the de minimis threshold to 60% only with regard to standards applicable to ARTs since only ARTs can, among other values and rights or combinations thereof, reference more than one official currency.

Accordingly, the EBA's interpretation of this chain of references concluding that the increased de minimis threshold in Article 45 (7) (b) must also apply to EMTs faces the following major counter-arguments:

1. Article 58 (1) (a) as the starting point of this chain of references does NOT refer to Article 45 (7).
2. The consequences of the proposed interpretation run counter the intention of the EU-legislator and counter the very objective of MiCAR. In such cases the interpretation of the level 1 legislative text must be guided by the ECJ's "effet utile" doctrine.
3. The wording of Article 45 (7) (b) provides, to say the least, a strong indication that the increased de minimis threshold is not meant to apply to EMTs but solely to ARTs.

We urge the EBA together with the European Commission to call upon their respective legal services for advice on the correct interpretation of the MiCAR level 1 text. The proposed draft RTS are based upon an interpretation that does not take into account the wording of Article 45 (7) (b) and is impossible to reconcile with the ECJ's "effet utile" doctrine. It would result in the exact opposite of the effect explicitly intended by the EU-legislator and to the very objective of MiCAR.

Question 1. Do respondents have any comment about the calibration of the percentages of reserve assets with specific maximum maturities as suggested in Article 1 and Article 2 of the draft RTS?

We do not oppose the setting of minimum percentages for investments in reserve assets with maximum maturities. However, we find the reference to the case of the Signature Bank for the 20%

minimum percentage proposed in Articles 1 (1) and 2 (1) far from compelling. In a number of respects the business model and risk profile of that bank bear little resemblance to the business models and risk profiles of issuers of ARTs or EMTs, which in turn can vary wildly across the potentially enormous range of issued ART and EMT products. Moreover, the size of Signature Bank (as of end-2022 total deposits of $88.6 billion and total assets of $110.4 billion) would suggest that a 20% minimum percentage should be applied to issuers classified as significant rather than to non-significant issuers. Instead, for significant issuers, Articles 1 (1) and 2 (1) set a minimum percentage of **40**%.

More importantly, it seems to us that also in this regard classification as significant or not tells little about the liquidity risks the minimum percentages set in Articles 1 and 2 are aimed to contain. The potentially very broad range of different business models and corresponding liquidity risk profiles call for a more flexible firm-specific approach combined with significantly lower mandatory minimum percentages. Competent authorities' case-by-case evaluation and risk assessment would surely also cover issuers' liquidity risk profile including the related stress testing practices and outcomes. On that basis concerns regarding not sufficiently conservative limits set internally by issuers could be addressed by firm-specific minimum percentages set by the responsible competent authority.

Question 2. Do respondents consider that the requirements in Article 1 and Article 2 related to the 1 and 5 working days maximum maturity could create excessive pressure in the repo market, taking into account the minimum required amount of deposits in credit institutions in the case of tokens referenced to official currencies?

The higher the de minimis thresholds for reserve assets meeting the 1 and 5 working days maximum maturity, the higher the likelihood that any necessary rebalancing of the reserve creates pressure in the repo market. That said, we're not aware of any evidence suggesting excessive pressure.

Question 3. Do respondents have any comment on the proposed approach in Article 3 of the draft RTS to not increase the minimum amount of deposits from 30% (or 60% if the token is significant) of the asset referenced in each official currency?

Regarding the 60% threshold set as de minimis threshold for bank deposits we refer to our comments above. This de minimis threshold should be abolished since it runs counter the very objective of MiCAR as the EBA's CP sets out very clearly. The proposal to set the 60% de minimis threshold at the same time as the maximum limit demonstrates the EBA's serious concerns regarding that amount of the reserve assets to be invested in bank deposits. We very much share these concerns. If the 60% de minimis threshold will be abolished, which we believe to be compelling, the maximum threshold for bank deposits should be set much lower. If the 60% de minimis threshold were not abolished we would urge the EBA to provide clarification as to how issuers are expected to manage compliance with a 60% threshold imposed at the same as de minimis and as maximum threshold. It is operationally impossible to always keep investments of the reserve of assets in bank deposits at the exact percentage of 60%.

Finally, we would welcome clarification by the EBA that reserve assets in the form of deposits safeguarded with a central bank of an EU Member State are to be counted towards the mandatory minimum percentage of bank deposits in the reserve of assets. We note in this regard that some EU central banks already allow for funds to be deposited by firms other than credit institutions and that the pending review of the PSD will introduce that possibility across all central banks in the EU.

Question 4. Do respondents have any comment with the definition of the requirement of a minimum liquidity soundness and creditworthiness in the deposits with credit institutions as proposed in Article 4 of the draft RTS?

The reference to issuers' internal risk assessment and risk appetite framework is welcome. However, the wording of Article 4 as it stands is not very clear at all. The related issues regarding the applicable concentration limits are set out below in our response to questions 5 and 6.

Question 5. Do respondents have any comment about the definition of the requirement of a maximum concentration limit of deposits with credit institutions by counterparty in Article 5 of these draft RTS? And about the definition of the general limit considering, in addition to deposit with a bank, also the covered bonds issued by and unmargined OTC derivatives with the same bank counterparty?

Question 6. Do respondents have any concern about compliance with these concentration limits in Article 5, considering in particular paragraph 14 of the cost/benefit analysis in relation to the potential operational burden and risk of a wrong direction diversification, linked to the minimum required liquidity soundness and creditworthiness of deposits with banks, and taking into account the minimum amount required of deposits with credit institutions by MiCAR for tokens referenced to official currencies?

We do have concerns regarding the related operational burden. However, much more importantly, we believe it is simply unrealistic that issuers will be able to comply with these concentration limits and contract banking services from as many credit institutions as required. The problems of payment institutions, electronic money institutions and FinTech firms handling virtual currencies to find credit institutions willing to offer banking services vital to their business operation and the provision of services to customers are well-know. They are due to what is commonly referred to as "de-risking". The EBA itself published in 2022 a "Report on De-risking and its Impact on Access to Financial Services" (EBA/REP/2022/01) providing in sections 3.2 (regarding payment and electronic money institutions) and 3.4 (regarding FinTech firms handling virtual currencies) numerous examples of credit institutions refusing to offer, or terminating on short notice the provision of, banking services. The EBA report sets out the disruptive impact de-risking has, including on the provision of services to the customers of these firms. It can be safely assumed that issuers of ARTs and EMTs will – and already do to an event greater extent - encounter the same problems in particular during the initial phase of building up their business and business operations towards economic viability.

Moreover, the wide-spread "de-risking" in the banking industry may well result in a negative selection regarding the remaining credit institutions willing to offer in the future banking services to issuers. For issuers subject to the 60% de minimis threshold, if retained, this means the credit risks associated with 60% of the reserve assets may well end up at the lower end of the credit quality available in the banking market. At the same time, the credit institutions willing to provide banking services to issuers may well be smaller institutions not meeting the size requirements referred to in Article 5 (1) of the draft RTS. Since for these credit institutions the maximum percentage is reduced from 10 to 5% of the reserve of assets non-significant and significant issuers would need to find in extremis 6 and 12 credit institutions respectively willing to provide banking services.

The additional limitations in Article 5 (2) and (3) and the extension provided for in Article 5 (4) to other risk exposures related to the same credit institution and all other entities to which it has close links, though as such not entirely unreasonable, further aggravate the problem.

We also note that the "de-risking" by many credit institutions may lead to a small number of credit institutions specialising on the provision of banking services to issuers of ARTs and EMTs. Such specialisation may occur for instance where a credit institution is under pressure to rapidly grow its business. The resulting sectoral concentration risk could give rise to interconnectedness and a high potential for contagion such that a crisis situation experienced by one issuer is transmitted via the credit institution to all other issuers relying on banking services provided by that same specialised credit institution.

Thus, the 60% de minimis threshold for bank deposits in combination with the proposed limitations of concentration risk would further increase the financial stability risks, which MiCAR and the proposed RTS are meant to contain.

In the PSD2 the problem of de-risking is addressed in Article 36 providing that "*Member States shall ensure that payment institutions have access to credit institutions' payment accounts services on an objective, non-discriminatory and proportionate basis*" and that "*credit institution shall provide competent authorities with duly motivated reasons for any rejection*". In this regard, the EBA in its Opinion published together with the 2022 report on concludes: "*… to address unwarranted de-risking and promote sound ML/TF risk management, further action by competent authorities and the co-legislators is required to support the effective implementation of provisions in existing EBA instruments and to address provisions that may be conflicting across Level 1 instruments going forward*." (para 17 in the related EBA Opinion). It also "*commits to following up with competent authorities on the steps they have taken to tackle unwarranted de-risking to inform the next EBA Opinion on ML/TF risks under Art 6(5) of the AMLD, which is due to be issued in 2023*." (para 12)

We urge the EBA to live up to its own recommendations and commitments. Regarding the proposed RTS it should reconsider and rework its approach to the de minimis threshold for bank deposits and to the related limitations of concentration risk. In order to assist the very objective of MiCAR thresholds and limitations that effectively contribute to increased financial stability risks should be removed.

Question 7. ***Do respondents have any comment about the definition of the mandatory over-collateralisation in Article 6 of these draft RTS and the rationale for it? Do respondents find it challenging from an operational perspective, in particular with respect to envisaging 5 days windows rather than 1 day windows for observation periods of the market value of the assets referenced versus the reserve of assets and over the previous 5 years? Please elaborate your response with detailed reasoning.***

As set out also in our response to the EBA Consultation Paper on Draft Guidelines establishing the common reference parameters of the stress test scenarios for the liquidity stress tests referred in Article 45(4) Regulation (EU) 2023/1114 we do not oppose the concept of mandatory overcollateralization. It seems to us reasonably well aligned to Article 36 (7) requiring that the "*aggregate value [of the reserve of assets] shall be at least equal to the aggregate value of the claims against the issuer from the holders of the asset-referenced token in circulation."*

However, there are issues that need further consideration and clarification:

- It is not obvious to us how to reconcile overcollateralization and the requirement under Article 36 (6) to "*ensure that the issuance and redemption of asset-referenced tokens is always matched by a corresponding increase or decrease in the reserve of assets*." Mandatory overcollateralization (as any additional overcollateralization required in the draft Guidelines referred to above) may well give rise, e.g. in the case of a redemption of ARTs or EMTs, for the issuer not to engage, as required according to Article 36 (6), in a corresponding decrease in the reserve of assets fully matching the redemption. Issuers may also choose when issuing additional ARTs or EMTs or independently of any redemption or issuance of tokens to acquire additional reserve assets in order to ensure the required or desired level of overcollateralization. Therefore, clarification is needed confirming that what issuers do or refrain from doing in order to ensure compliance with mandatory or any required additional overcollateralization does not infringe the requirements according to Article 36 (6). This is all the more important given the obligation of issuers under Article 36 (8) to have "*… a clear and detailed policy describing the stabilisation mechanism …"* including according to Article 36 (8) (d) a description of "*the procedure by which the asset-referenced tokens are issued and redeemed, and the procedure by which such issuance and redemption will result in a corresponding increase and decrease in the reserve of assets*". That policy would have to set out instances where the build-up of the mandatory overcollateralization and, as the case may be, any additional collateralization beyond the mandatory minimum does require not compliance with Article 36 (6). The EBA should state clearly that mandatory over-collateralisation takes precedence over compliance with Article 36 (6). We note in this regard that the requirement in Article 36 (6) appears to us to be closer aligned to the concept underlying the definition of ARTs and EMTs in Article 3 (6) and (7) than the requirement under Article 36 (7).
- It is also important to bear in mind the link between overcollateralization and own funds requirements. Overcollateralization necessarily results in a higher average amount of the reserve of assets thus generating higher mandatory own funds requirements under Article 35 (1) (b).

Accordingly, competent authorities when assessing an issuer's overcollateralization should also take into account its capitalization and acknowledge that own funds above the own funds requirements can be as effective as overcollateralization in containing the de-pegging risk. Issuers, in particular if well-capitalized, should be free to manage the level of overcollateralization not least with a view to the impact it inevitably has on own funds requirements and the margin by which the issuer meets these requirements.

Question 8. Do respondent think that any provision in the draft RTS is confusing and that some clarification would be necessary?

- see comments above

Members of the EMA, as of January 2024

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