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CLIENT ALERT

Navigating MiCAR: Key Insights for Crypto Asset Service Providers

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Since 30 December 2024, the European Markets in Crypto-Assets Regulation (Regulation (EU) 2023/1114, "**MiCAR**") is applicable in all 27 EU Member States as the first comprehensive and harmonized regulatory framework for crypto-assets and has resulted in a significant transformation of the regulatory landscape.

In particular, MiCAR has introduced its own authorization regime for crypto-asset service providers ("**CASPs**"), which generally applies to any firm actively marketing crypto-asset services to European customers. Once authorized in one EU Member State, CASPs can provide their services to customers located in any EU Member State by way of MiCAR's passporting regime. However, non-EU firms must set up an EU-registered entity for the purpose of obtaining a MiCAR authorization. Otherwise, the only way for a non-EU firm to service European customers is by relying on the so-called "reverse solicitation" regime, based on which firms may provide services initiated at the own exclusive initiative of the European customer.

Recently, the European Securities and Markets Authority ("**ESMA**") has published two papers with particular relevance for market participants in the crypto sphere: first, a supervisory briefing regarding the authorization of CASPs under MiCAR on 31 January 2025 (the "**CASP Briefing**") and, second, guidelines on reverse solicitation under MiCAR on 26 February 2025 (the "**Reverse Solicitation Guidelines**"). With the CASP Briefing ESMA

provides mere explanatory guidance in order to further supervisory convergence for a harmonized application of MiCAR by national competent authorities ("**NCAs**"). In contrast, the Reverse Solicitation Guidelines entail generally binding interpretations of ESMA, and NCAs need to apply such guidelines unless they notify ESMA that they do not intend to comply with them.

On the basis of the CASP Briefing and the Reverse Solicitation Guidelines, we provide answers to some of our clients' most frequent questions on governance, outsourcing and reverse solicitation in connection with providing crypto-asset services.

Q1: Is it permissible for a CASP's management board to be located outside of the EU Member State in which the CASP is authorized?

CASPs require sufficient in-country personnel and at least one executive management board member located in the EU Member State in which the CASP is authorized. However, if the CASP is authorized in a small EU Member State (< 1 million inhabitants, such as Malta and Luxembourg), regulatory authorities might allow an executive management board member to be based in a different Member State. In this case, the board member must be available at short notice (no more than two business days) for appearing in person before the NCA.

Q2: May a CASP be operated or governed from elsewhere from an EU regulatory perspective?

NCAs are supposed to require CASPs to demonstrate sufficient "governance and substance" in their jurisdictions of authorization to allow them to exercise effective supervision and ensure compliance with applicable regulations. For example, in cases where a CASP is governed, managed and operated from outside of the EU, there may be doubts as to whether supervisory authorities are able to effectively monitor their activities. According to ESMA, in terms of governance, CASPs need to have the power to autonomously make decisions on their EU policy and this should be reflected in the reporting lines within the CASPs. For example, a setup in which CASPs operate within a group structure with relevant group entities and/or leadership operating outside the EU-regulatory scope is more likely to be viewed critically.

In terms of substance, arrangements where functions are performed by or for the EU entity outside the EU should be scrutinized. The factors to be considered as part of this assessment are **(i)** the number of functions performed outside the EU; **(ii)** the importance of these functions (e.g. supporting functions such as IT support and HR support are more likely considered acceptable); and **(iii)** the percentage of total costs spent on these functions. Overall, setups where the substance of the CASP, either on a management or on an operational level, is limited should be carefully considered.

Q3: May a CASP's staff be located outside the Member State of its authorization?

Generally, a CASP's staff may be located elsewhere; however, it needs to be considered whether this impairs the CASP's ability to ensure continuity and regularity in the performance of its crypto-asset services. As part of this assessment, the roles of the staff based outside the Member State as well as the

concentration of such staff at certain functions needs to be taken into account. Structural setups which **(i)** prevent the exercise of the supervisory functions of the national regulator; **(ii)** prevent prompt access to relevant information; **(iii)** prevent management from exercising effective control over staff members; and **(iv)** undermine the CASP's capacity to operate in a continuous and regular manner are prohibited.

Q4: May the members of the management board simultaneously hold a role in the management of the CASP's parent company or does this raise concerns with the regulator?

According to ESMA, "dual hatting" structures raise the concern whether the manager "wearing multiple hats" is able to commit sufficient time to the CASP, especially if it is of considerable size and complexity. Therefore, the respective managers' role with the parent company should not impair their ability to devote at least 50% of their time to effectively fulfil their responsibilities with the CASP. In the case of a CASP's CEO, ESMA's requirements are stricter (cf. Q5, below).

Q5: Is it acceptable for a CASP's CEO to take up a further management role from a regulatory perspective?

In the case of a CASP's CEO, ESMA's requirements for "dual hatting" structures are stricter than in the case of other management board members.

First, as a rule of thumb regarding the necessary time commitment, a CASP's CEO should be able to devote 100% of his or her time to CASP duties. However, if the CASP can demonstrate to the regulatory authority that the CEO's further commitments do not negatively impact his or her ability to effectively govern the CASP in a compliant way, the NCA may allow a lower time commitment.

Second, the regulator might raise concerns whether the CEO's role with the CASP's parent company may interfere with the independent functioning of the CASP itself. In this regard ESMA underlines, in particular, that the chair of the management board of a CASP should be generally independent.

As a consequence, if the CASP's CEO is supposed to also take up other management roles within the CASP's group, firms should first assess the size and complexity of the CASP and the other entity. Based on such assessment, the roles and responsibilities of the CASP's CEO as a manager of the other group entity must be clearly defined in order to **(i)** secure a sufficient time commitment for the CEO's CASP duties, **(ii)** avoid any conflicts of interest between the roles, and **(iii)** limit the CEO's decision-making power when acting for the CASP's group company in respect of all decisions affecting the CASP.

Q6: What regulatory requirements must the executive management board members of a CASP fulfill?

According to ESMA, a CASP's executive management board members should: **(i)** be aware of national rules of the Member States in which the CASP is located or provides a significant level of services; **(ii)** have knowledge of EU-market idiosyncrasies and awareness of the distinctive characteristics of the national

market; **(iii)** have relevant prior work experience (ideally in the same sector and ideally in the EU); and **(iv)** have at least a good level of understanding of the technical functionalities of crypto-assets and the crypto-asset services provided. ESMA suggests that executive management board members with less management experience can, in principle, be compensated for by executive management board members with more management experience in the regulated finance industry.

Q7: Which factors does ESMA consider relevant to the permissibility of outsourcing arrangements?

As a key principle, EMSA emphasizes that outsourcing arrangements should not involve the delegation of functions to the extent that a CASP becomes a letter-box entity or an empty shell. Outsourcing arrangements should be assessed, amongst others, according to the following criteria: **(i)** number of the outsourced functions; **(ii)** importance of the outsourced functions; **(iii)** percentage of total costs spent on outsourced activities; **(iv)** whether NCAs are able to obtain information from the entity performing the outsourced functions (if not, such a setup would be incompatible with MiCAR); **(v)** whether the CASP will be able to effectively control and monitor the outsourced activities; and **(vi)** whether a cooperation agreement between the EU NCA and a third-country national authority of the outsourced functions is required.

Against this background, the outsourcing of relevant functions, such as information and communication technology (ICT) infrastructure building and management, will be critically assessed by the NCAs. In addition, a complete outsourcing of highly important functions like risk management, compliance, or key management functions is generally not acceptable as it will likely jeopardize the effective supervision of the CASP. Therefore, only certain elements of such activities might be outsourced, as they are crucial to a robust and substantive operation within the EU.

Q8: Which promotion activities of third-country firms are regarded as client solicitation and prevent such firms from relying on the reverse solicitation exemption when providing crypto-asset services to EU customers?

Generally, ESMA construes the concept of solicitation of clients by third-country firms broadly. Relevant solicitations include promotions, advertisements and press releases by any means concerning crypto-asset services. However, relevant solicitations can also comprise promotions, advertisements and marketing campaigns of a general nature that are meant to create brand awareness without mentioning any specific service. In particular, the participation in road shows, invitations to fill in a response form or to participate in a training course and the sponsorship of EU- or Member State-centric sporting events may qualify as a solicitation of clients. According to ESMA, even the fact that a third-country firm operates a website or parts thereof in an official language of the EU which is not customary in the sphere of international finance might indicate that the firm is targeting EU clients. Also, the use of regional- or country-specific search engine optimization strategies or geo-targeting strategies for running digital ads could indicate the solicitation of EU customers.

Q9: Which third parties' activities are relevant for determining whether a relevant client solicitation has taken place?

According to ESMA, solicitation may occur irrespective of the person through whom it is performed and can particularly be carried out by third parties acting on behalf of or having close links with the third-country firm. It does not matter whether such relation is based on a contract or on an implicit informal agreement. For example, third-party endorsers can include so-called influencers who direct the audience to the third-country firm's website, provide means of access to the services offered or display the third-country firm's logo. Also, the provision of crypto-asset services following solicitation on behalf of a third-country by a person or entity regulated in the EU should still be regarded as a breach of MiCAR.

Q10: Do contractual provisions between the third-country firm and the EU customer, such as clauses stating that the business relationship was established upon the exclusive initiative of the customer, prevent the characterization of the firm's activities as client solicitation?

No. According to ESMA, the assessment whether or not the crypto-asset service or activity is provided at the own exclusive initiative of the client should be purely factual and facts cannot be superseded by contractual arrangements or disclaimers.

Q11: Once a business relationship has been established between a third-country crypto service provider and an EU customer upon the exclusive initiative of the EU customer, can the third-country service provider continue providing services to this customer without becoming subject to MiCAR's authorization requirements?

According to ESMA, the time at which the third-country firm is approached by the EU customer must coincide closely to the time at which the respective crypto-asset service is marketed and provided to this customer. More specifically, ESMA states that if an EU customer contacts the third-country firm to buy a crypto-asset, the firm may at this time market crypto-assets of the same type to this customer. However, the third-country firm might be held to solicit clients if it markets further crypto-assets to the same customer one month later (even if these crypto-assets are of the same type as those which were originally marketed). In other words, the principle of reverse solicitation allows a service provider to provide services in a specific situation, but does not initiate client relationships based on which services can be provided on a sustained basis.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

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