

► FEATURE

CRYPTOASSETS

Regulation vs. innovation: the cryptoverse challenge

Cryptoassets hit a major milestone in November 2021 when their total market cap exceeded \$3 trillion. New use cases are emerging, and one country has even adopted bitcoin as legal tender. As cryptos work to win over a wider public, a balance needs to be struck between regulating this new universe and letting innovation flourish.



► EDITORIAL Stéphane Giordano and Bertrand de Saint Mars | AMAFI

The European Commission has published a major new legislative package, a year after releasing a plan to relaunch the Capital Markets Union, or CMU. The new proposals include the European Single Access Point (ESAP) Directive, which aims to create a single platform for financial and sustainability-related information on listed companies. The package also comprises reviews of the European Long-Term Investment Funds (ELTIFs) Regulation and the Alternative Investment Fund Managers Directive (AIFMD), as well as the Markets in Financial Instruments Regulation (MiFIR), which underpins the functioning of Europe's markets (see *News* p. 6).

These proposals are crucial to reinvigorating CMU and enabling the European Union to develop its open strategic autonomy. They aim to support the economic recovery while helping the EU meet the financing needs associated with the green and digital transitions as well as an ageing population. Meanwhile, with the United Kingdom kicking off

discussions around its Wholesale Markets Review, the Union must also contend with a powerful competitor on its doorstep. This is especially important because the UK is demonstrating impressive regulatory agility and taking an unabashedly pragmatic stance in its bid to attract European investors and issuers.

AMAFI therefore welcomes this boost for CMU. Talks are due to begin shortly within the European Parliament and Council, and this issue must not be overlooked. Once again, we need to hammer home that business competitiveness and an attractive regulatory framework are included alongside financial stability, market integrity and investor protection (*AMAFI / 21-38*) at the heart of the discussions. The European Union is not merely a market of consumers. The pressing need to safeguard and grow our autonomy means that the EU must also be a market of robust and competitive producers.

Regulation vs. innovation: the cryptoverse challenge

 Sandra Sebag

Cryptoassets have spread to every corner of finance, along with their colourful jargon: think laser eyes (investors with bullish sentiment) and diamond hands (those reluctant to sell). Since the 2009 launch of the first cryptocurrency, Bitcoin, the industry has gone from strength to strength. The capitalisation of the global crypto market has skyrocketed in recent months, breaking the \$3 trillion mark in November, up from \$500 billion just one year ago. And the possible uses of cryptoassets have expanded to the point that they are appearing everywhere, from investment and financing to insurance. As a result, the cryptoverse is becoming more complex and harder to characterise. The instruments themselves are variously referred to as cryptocurrencies – even though they do not perform all the functions assigned to fiat currencies – or cryptoassets, since they can be used for activities other than financial services. What they all have in common is the distributed ledger technology, or blockchain, that underpins the transactions.

Salvation of El Salvador?

Cryptocurrencies were initially developed as alternatives to the major currencies and gold. One of the best-known examples is Bitcoin. In September 2021, El Salvador became the first country in the world to adopt the crypto as legal tender. A small Central American nation relying for 20% of its income on remittances from its US-based diaspora, El Salvador is at the mercy of American taxes, the dollar price and the fees charged by financial intermediaries. Bitcoin could change all that. Moreover, within one month of adopting it, the country had three million Bitcoin current accounts, or twice the number of existing bank accounts. With the El Salvador experience, Bitcoin may be achieving one of its primary goals: to promote financial inclusion by enabling unbanked and under-banked people to access bank accounts, conduct transactions and get loans. It is important to bear in mind, though, that El Salvador went ahead with its initiative at a time when the Bitcoin price was surging.

New applications

Two major new crypto trends have emerged in the past year or so: stablecoins and decentralised finance. Stablecoins are cryptocurrencies backed by a legal currency, typically the US dollar. USD Coin is a stablecoin issued by Coinbase, a cryptocurrency exchange platform. One USDC can always be redeemed as one US dollar, which keeps the value stable. Since stablecoins are pegged to a strong currency, they are far less volatile than other cryptocurrencies, making them more suitable for use in a wide variety of transactions. Combining the benefits of crypto with the stability of fiat currencies, stablecoins are enjoying surging popularity. But they are also coming under increasing regulatory scrutiny.

Decentralised finance, or DeFi, is driven by a revolutionary idea. It allows people and organisations to engage in financial transactions – borrowing money, taking out insurance, accessing investments and other services – without having to go through a financial intermediary. A pair of counterparties, which could be two individuals, or a business and an individual, reach an agreement on a deal. Transactions between the two are based on a protocol or algorithm designed by a fintech or private individual and made openly available. These transactions are entered into a blockchain, making them both traceable and secure. DeFi's protocols thus replicate mechanisms similar to those of conventional finance, but in a way that is both decentralised and universally accessible. From small-scale beginnings less than a year ago, decentralised finance is growing exponentially and has exceeded the \$100 billion mark. That said, these protocols are still settling in and have yet to win over a broad public. Furthermore, they lack a specifically tailored regulatory framework to prevent misuse.

Traditional firms point to the risks raised by the emergence of unregulated financial service providers. "Like any form of recent technological innovation at the start of its regulatory journey, the crypto industry is regulated with a light touch, which makes it vulnerable," says Emmanuel ►►

►► de Fournoux, AMAFI's Director of Market Activities. "The fact that no intermediaries participate in executing the protocols, plus the fact that crypto bypasses certain rules, means that the regulator cannot perform its essential role as watchdog." But, as Mr de Fournoux points out, France's central bank is pursuing several initiatives as it explores the transformative potential of technological innovations in the financial sector, including regulating the development of cryptoassets. "The Banque de France is rightly pushing ahead with trials that test interactions between blockchain solutions and traditional players with a view to consolidating the development ecosystem for new technologies that will benefit finance," he concludes.

Regulating crypto: France blazes a trail

Many conventional financial participants are keen to invest in these solutions as they seek to gain a foothold in crypto. Some countries are actively encouraging innovation in these areas, while others are trying to impose stringent curbs. France belongs to the first group. Alive to the rapid growth of fintechs and their associated ecosystem, France pioneered the first regulatory framework for cryptoasset activities and established a bespoke regime for digital asset services providers, or DASPs, under the Action Plan For Business Growth and Transformation Act that came into force in late 2019. Firms offering digital asset services must now register with the national securities regulator, AMF, and show that they can fulfil due diligence obligations, especially those aimed at deterring money laundering. Already, 25 firms have been registered in France. "We were the first firm to be AMF-registered. The dedicated regulatory framework gives our sector real legitimacy and allows us to do business with

traditional players," explains Romain Saguy, marketing and commercial director at Coinhouse, one of France's main cryptoasset platforms. Oliver Yates, CEO of Sheeld Market, a French fintech that offers to plug institutional investors straight into the crypto universe, says "We deal with firms in Asia, particularly Singapore and Hong Kong, as well as in English-speaking countries. They are reassured by the fact that we are registered in France. Having DASP status is definitely beneficial". Yet all is not smooth sailing for those looking to fly the crypto flag. Banks often refuse to open accounts for companies that do business in cryptocurrencies. In addition, AMF registration is a time-consuming process, while in the meantime unregulated firms are engaging in unfair and unlawful competition in France.

Other jurisdictions are paying attention too, as they seek to balance the need for adopting additional regulation against the risks of curbing invention. Testifying on 14 September to the US Senate Banking Committee, the Chair of the Securities and Exchange Commission, Gary Gensler, said that America had insufficient investor

protection in crypto finance, issuance, trading and lending. He likened the situation to the Wild West and described crypto as rife with fraud, scams and abuse in certain applications. The SEC is working with the CFTC, the Federal Reserve and other US financial regulators on ways to protect investors on these markets and identify regulatory gaps to be filled. In November, meanwhile, the Fed, the Office of the Comptroller of the

Currency, and the Federal Deposit Insurance Corporation announced that they had conducted a series of joint policy sprints with a focus on cryptoassets. Treasury Secretary Janet Yellen has called for rules to be adopted quickly. ►►

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France pioneered the adoption of the first regulatory framework for cryptoasset-related activities
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▶▶ The United Kingdom is likewise in the process of developing its approach. The Financial Conduct Authority is the country's main crypto regulator. FCA Chair Charles Randell has said that while useful innovation needs to be supported, online platforms should expect a future where regulation addresses the significant risks they pose, in the same way as other businesses: "Same risk, same regulation" is the mantra. Since January 2020, the FCA has registered cryptoasset firms under anti-money laundering regulations, and in June 2021 it issued a consumer warning about Binance, a crypto exchange. In early 2021 the UK Treasury held a consultation on the UK's regulatory framework for cryptoassets and stablecoins.

MiCA: the good and the bad

There are fears that Europe's draft Markets in Cryptoassets Regulation, or MiCA, might disrupt France's supportive climate. The effects on DeFi and stablecoins are flagged as particular concerns. The proposal for a new regulation, which is unlikely to come into effect before 2023 or 2024, was filed by the European Commission in September 2020 and takes its cue from France's approach. As in the French framework, other countries will require service providers to be registered, and the types of firms that can be classified as DASPs will be the same as those on the French market. In this sense, French firms enjoy a theoretical edge in terms of preparedness for the new rules.

But critics claim that in seeking to regulate crypto participants in the same way as conventional financial firms, the proposed regulation fails to consider recent developments and the sector's specific features. Decentralised finance is an area of concern. In a sector where innovation is key, there are fears that MiCA could stifle the emergence of new participants. Instead of being organised by a company or an intermediary, DeFi exchanges are handled by an automated process. Once the protocol has been created and made publicly available, transactions are processed automatically. So

how can standard Know-Your-Customer requirements apply? Thibaud Boutrou, COO of JustMining, a blockchain investment expert, says that the Commission is looking to tackle DeFi without taking the time to understand the complex issues or giving DeFi time to mature. "Decentralised finance needs time to grow up," he says.

Some fintechs complain that the European proposals could stunt their growth. They stress that while regulators cannot stop DeFi from developing, they can prevent it from taking root in Europe and, possibly, drive it towards more welcoming jurisdictions. Some firms are thinking about completely retooling. Kriptown, a specialist in capital financing for startups through digital issues, is one such firm. Its chairman and founder, Mark Kepeneghian, cautions: "Once MiCA comes into force in Europe, we will look at the options for changing the way we operate in order to be compliant. But we might also seek to be covered instead by the pilot distributed ledger technology regime currently under discussion in the European Parliament. This initiative, still in its infancy, will apply to market infrastructures using DLT to support automated securities settlement systems".

The treatment of stablecoins is another source of worry, again amid concerns about derailing innovation. The proposed rules are extremely strict because they were designed for major groups, such as Meta, formerly Facebook, which is working on a stablecoin project dubbed Diem (previously Libra). But smaller companies, which are often dynamic innovation drivers, also need to be able to flourish, which they may struggle to do under the proposed new framework. At a time when 99% of stablecoins are pegged to the US dollar, this approach could see Europe lose ground in the stablecoin competition, depriving it of a digital currency with a solid international presence.

Striking the right balance between regulating an emerging universe and unleashing innovation presents considerable challenges. No need for laser eyes to see that.

IOSCO

IOSCO Annual Meeting and ICSA meetings, 8-16 November 2021

The 2021 annual meeting of the International Organization of Securities Commissions (IOSCO) was cancelled due to the Covid-19 pandemic and replaced by a series of virtual meetings held in November 2021.

As part of the gathering, the International Council of Securities Associations (ICSA) organised a virtual bilateral meeting between finance industry representatives and several chairs of IOSCO committees.

The meeting broached a number of priority areas for IOSCO, such as raising the level of professionalism in sustainable finance and the need for global standards to enable different markets to interact more effectively. The meeting also covered other key concerns for IOSCO, notably the impact of Covid-19 on secondary-market functioning, risks connected with the development of the OTC derivatives market, and the challenges posed by the development of cryptoassets, the rise of neo-brokers and growing cybersecurity challenges.

Arnaud Eard

MIFID II

Remuneration

The AFG, AMAFI, ASF and FBF submitted a joint response ([AMAFI / 21-62](#)) to ESMA's consultation on updating the guidelines on MiFID II remuneration requirements.

The co-respondents stressed that the proposed updates were redundant because virtually all the topics are addressed by existing directives, such as CRD IV, UCITS, AIFMD and IFD. They also pointed out that the proposed scope is much too broad, as it encompasses staff who are involved directly or indirectly in the distribution of financial instruments. In practical terms, this would affect several tens of thousands of people in international groups, creating senseless implementation challenges that would do little to support the risk-control efforts that originally spurred the requirements.

Since the UK is clearly determined to review some of the rules arising from European regulations, the co-respondents also underlined the need to consider how Brexit might affect the ability of EU firms to attract the talent that will safeguard and boost their competitiveness.

Arnaud Eard

CMU

Business competitiveness and attractiveness of the European regulatory framework

AMAFI has been stressing for months the need to consider the competitiveness of European firms and the attractiveness of the regulatory framework in connection with the CMU reboot ([AMAFI / 21-38](#)).

To convey this message, an AMAFI delegation led by Stéphane Giordano met with Florian Denis from the office of Mairead McGuinness, the European Commissioner for Financial Services. The discussion centred around several key issues: the MiFID II/MiFIR revision and the DTO, introduction of a consolidated tape ([AMAFI / 21-28](#)), the inducements regime ([AMAFI / 21-48](#)), and access to UK central counterparties (CCPs).

Mr Denis emphasised the importance of finding a solution so that European banks operating in the UK are not simultaneously subject to the European and UK DTOs. He indicated his backing for a near real-time CT and said that the Commission had not yet determined its position on inducements. On access to UK CCPs, he said the temporary equivalence would be extended to early 2022 and that the Commission would adopt measures in 2022 to repatriate liquidity to the Union.

Arnaud Eard

MIFID II REVIEW

MiFIR Review

The European Commission adopted on 25 November the proposal to review the Markets in Financial Instruments Regulation. The introduction of a European consolidated tape (CT) is a central plank of the new framework and a key policy issue for the Commission. The new CT will provide near real-time pre- and post-trade data for equities and post-trade data for bonds. On the sensitive matter of market-data costs, the proposal calls for a regulatory technical standard (RTS) to clarify the “reasonable commercial basis” concept.

Other key reforms will bring tougher restrictions for multilateral trading facilities and systematic internalisers on the equity market, while the transparency regime for bonds is also set to be strengthened and deepened.

With the branches of European firms still at a competitive disadvantage owing to the dual application of European and UK derivatives trading obligations (DTOs), Member States will be able to ask the Commission to suspend the European DTO under certain conditions. The proposal also transposes ESMA’s [clarification](#) about the scope of the share trading obligation.

MiFIR transparency regimes

AMAFI responded to ESMA’s consultation on the review of MiFIR transparency regimes ([AMAFI / 21-57](#)). Overall, it welcomed most of the proposals to streamline reporting and improve

the identification of transactions. Harmonisation efforts should help to identify addressable liquidity and distinguish “technical” trades from price-forming ones. This is a significant step forward, not to mention a pre-requisite for establishing a European consolidated tape.

Conversely, AMAFI pointed out that the proposed amendments to the transparency rules for ETF trading fall within the scope of Level 1 measures and should not have been included in the technical consultation. It also drew ESMA’s attention to the potential costs associated with the proposed changes and called for the modifications to be conducted in a manner consistent with the MiFIR review.

Best execution reports

On 24 September 2021 ESMA began a consultation on best execution reports ([ESMA35-43-2836](#)) in which it suggested amendments to the current arrangements as part of the MiFID II review. The proposals include technical amendments to RTS 27 and 28, which set best execution reporting requirements for execution venues and investment firms, respectively.

As regards execution quality reporting by trading venues (RTS 27), AMAFI said the proposed overhaul would not make the disclosures more meaningful, and it called for these reports to be scrapped, as they include redundancies with existing mechanisms used by institutions to determine their best execution policy.

AMAFI also reiterated its general position on execution quality reporting by investment firms (RTS 28) ([AMAFI / 21-35](#)).

In AMAFI’s view, these reports are not sufficiently valued by customers: wholesale customers have their own execution analysis systems, while the disclosures are too technical to be considered useful to the retail segment. Accordingly, these reports, too, ought to be scrapped. However, if they are kept, AMAFI supports some of the amendments proposed by ESMA, such as the clarifications on best selection reporting and the elimination of the distinction between “passive” orders that provide liquidity by indicating a willingness to buy or sell and “aggressive” orders that absorb liquidity through execution in the order book.

Inducements KPMG study

As part of the MiFID II review, but putting the focus on inducements, KPMG finalised its study on inducement practices, including the resulting costs for investors. The consulting firm was commissioned to carry out the research by several French and European industry associations, including AMAFI.

The study looked at the total cost of ownership, understood as incorporating all costs linked to acquiring the product, including advisory costs, in a distribution model with inducements and in a fee-based distribution model in which inducements are banned. It also assessed additional services provided to customers plus conflict-of-interest management arrangements established for the model with inducements.

The study will be released in mid-January.

Arnaud Eard, Emmanuel de Fournoux, Pauline Laurent, Mehdi Ounjema

SUSTAINABLE FINANCE

Climate indices



Before the summer, the AMF consulted AMAFI on how Climate Transition Benchmark and Paris Alignment Benchmark (CTB / PAB) indices should be treated with regard to the complexity restrictions set out in *AMF Position No. 2010-05*, where the indices are used as underlying instruments for structured products issued as euro medium-term notes.

While wholeheartedly supporting the AMF's initiative, AMAFI proposed some wording changes for the draft update of Position No. 2010-05 (*AMAFI / 21-55*), which were welcomed by AMF staff. The amended position is scheduled to be published before the end of the year.

Mapping sustainable finance

AMAFI published its sustainable finance mapping project in July (*AMAFI / 21-43*). The initiative is intended to support members as they analyse and keep track of sustainable finance-related rules, while providing an overview of European and French legal provisions, as well as of the work currently being done by the various competent authorities.

However, the entry into force of new legislation over the summer, including delegated acts incorporating sustainability factors into the MiFID II framework (Delegated Regulation (EU) 2021/1253 & Delegated Directive (EU) 2021/1269, cf. *AMAFI / 21-50 & 21-51*), meant that an update was required (*AMAFI / 21-60*). The document will continue to be monitored on a regular basis.

Thiebald Cremers, Pauline Laurent, Adélaïde Fischmeister, Mathilde Le Roy, Léah Moyal

MIFID II

Quick Fix

In October 2021, AMAFI provided the French Treasury with comments on the transposition of Directive (EU) 2021/338 amending MiFID II, known as the MiFID II Quick Fix Directive (*AMAFI / 21-58*). Member States had until 28 November 2021 to transpose the directive into domestic law.

Besides mentioning some minor changes, AMAFI alerted the authorities to inconsistencies between the Quick Fix and Delegated Regulation (EU) 2017/565 supplementing MiFID II, which also appear in the transposition draft. The final document is due to be published in the Official Journal in the coming weeks.

Thiebald Cremers, Mathilde Le Roy, Léah Moyal

ANTI-MONEY LAUNDERING

Cross-sector executive order on internal control

AMAFI prepared a draft Q&A on the cross-sector executive order on anti-money laundering/counter-terrorist financing arrangements and internal control, asset freezes and the ban on using or making available funds or economic resources (Executive Order of 6 January 2021). The draft was sent to the ACPR at end-October for an opinion.

AMAFI also asked the ACPR to clarify a number of points, including its guidelines on customer identification, ID verification and KYC aspects, registries of trust beneficial owners, and European Banking Authority guidelines on money laundering risk factors ([EBA/GL/2021/02](#)), with which the ACPR declared itself to be compliant in early October.

EBA draft guidelines

AMAFI examined EBA's consultation on its draft guidelines for AML Compliance Officers. While AMAFI welcomes efforts to promote European-level harmonisation of practices relating to AML functions, it called on EBA to consider current legislative work being done by the Commission, especially the draft AML/CTF regulation, in order to promote better regulatory stability in this area ([AMAFI / 21-59](#)).

European Commission package of AML/CTF legislative proposals

AMAFI responded to two of the four consultations launched by the European Commission following the publication on 20 July of a package of [legislative proposals](#) aimed at strengthening Europe's rules on anti-money laundering/counter-terrorist financing. AMAFI's response focused on the Commission's draft AML/CTF regulation and the proposed Sixth Anti-Money Laundering Directive ([AMAFI / 21-63](#)).

In its feedback, AMAFI raised a number of issues flagged by members, including the significant step-up in obligations to identify and verify the identity of beneficial owners, the Commission's proposed policy for third countries and laundering threats, and the definition of a correspondent relationship.

Adélaïde Fischmeister

VAT

Treatment of commodity derivatives

Discussions on the VAT treatment of derivatives on cash- or physically-settled commodities or goods, previously handled by AMAFI's Tax Committee, are continuing in dedicated groups. Initially begun to address issues connected with the relocation to France of activities previously carried out in the UK, this work is intended to specify the scope of the VAT exemption applicable to these transactions.

Since AMAFI felt unable to obtain a clear and reliable operational response from a direct reading of the legal and policy framework, it wrote at end-October to France's Tax Legislation Directorate requesting confirmation of its analysis. The authorities are expected to issue a response in the coming weeks that should provide participants with the necessary legal certainty.

Eric Vacher, Maguette Diouf

EMPLOYMENT

Representing employers

Regarding employer representation arrangements, AMAFI has been recognised, as it was four years ago, as the sole organisation representing employers in financial-market activities, under collective bargaining agreement No. IDCC 2931, for the 2021-2024 period by an Executive Order dated 6 October 2021 and published in France's Official Journal on 7 November 2021.

Alexandra Lemay Coulon,
Ashley Berne

NEW MEMBER



► **Cohen & Company Financial (Europe) SA**, an investment firm whose activities include order reception-transmission-execution, portfolio management and investment advice. Paul Vernhes (Chief Executive Officer) is its senior manager.

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AMAFI documents quoted in this Newsletter and flagged with a reference number are on our website at

www.amafi.fr

Most of them, notably AMAFI's responses to public consultations, are freely available, but some are restricted to members only.



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