

Interactions between the Payment Services Directive (PSD) and the Market-in-Crypto-Assets Regulation (MiCA)

1. Preliminary remarks

Following the partial implementation of the Market-in-Crypto-Assets (MiCA) Regulation¹ on June 30, the rules applicable to stablecoins came into effect, marking a significant step in the regulation of crypto-assets within the European Union. However, the industry is currently concerned about certain regulatory implications recently highlighted by the Association: issues of interpretation and coexistence of the text with the Payment Services Directive (PSD2), particularly regarding stablecoins, or electronic money tokens (EMTs), are emerging.

In summary, the identification of stablecoins, "EMTs," as "funds" under PSD2 is likely to increase the requirements applicable to issuers and Crypto-Asset Service Providers (CASPs) that handle them, potentially obliging them to obtain specific licenses despite already being subject to authorization under MiCA.

In this context, this article provides a simple analysis of the interactions between PSD2 and the MiCA Regulation, highlighting the operational and regulatory challenges for CASPs.

2. History of PSD/MiCA regulations

2.1. The Payment Services Directive (PSD)

Initially, the first directive (PSD1) adopted in 2007 and implemented in 2009 aimed to standardize payment services in the European Union and enhance competition by encouraging the entry of new providers into the market. PSD2, adopted in 2015 and implemented in 2018, furthered these goals by introducing additional rules to improve the security of online payments, protect consumers, and promote innovation, notably through Open Banking.

At the time, PSD2 laid the foundation for a more modern regulatory framework for payment services across Europe. However, the evolution of asset classes, particularly the rise of crypto-assets in recent years, has led to ongoing reflection on its capacity to adapt to these new challenges.

¹ <https://eur-lex.europa.eu/legal-content/FR/TXT/PDF/?uri=CELEX:32023R1114>.

On June 28, 2023, the European Commission submitted a proposal to revise the Payment Services Directive (PSD) and establish a new Payment Services Regulation (PSR) to unify and modernize this regulatory framework. Yet, recent interpretations regarding the regulatory treatment of stablecoins, when classified as electronic money (thus as "funds"), contradict what is provided in the MiCA regulation.

The Association has repeatedly argued that the interpretation of the rules governing EMTs under PSD2 should be clarified to resolve the legal uncertainty faced by issuers and actors handling EMTs.

2.2. Market-in-Crypto-Assets Regulation (MiCA)

The Market-in-Crypto-Assets Regulation, commonly referred to as "MiCA," is another European Union initiative aimed at filling the regulatory gap surrounding crypto-assets. Before MiCA, crypto-assets were primarily governed by varying national regulations, leading to market fragmentation and uncertainties for businesses operating in this field. Adopted in 2023, MiCA thus provides the first European regulatory framework for crypto-assets, Crypto-Asset Service Providers (CASPs), issuance of tokens other than stablecoins, and issuance of stablecoins (ARTs/EMTs). The text also regulates practices of market abuse and manipulation when related to crypto-assets.

3. Issues arising from the joint application of PSD2 and MiCA

EMTs represent a "type of crypto-asset" designed to "maintain a stable value" and are generally "backed by a single fiat currency." Several MiCA formulations assert this while specifying that, due to certain functional similarities, they may **sometimes** be considered electronic money.

Example: Tether (USDT) / USD Coin (USDC).

MiCA then provides that payment services regulation (PSD) should apply to EMT issuers and CASPs only in strictly limited cases, specifically in cases of (i) public offering or (ii) admission to trading of these assets.

Definition of crypto-assets under MiCA - Article 3, paragraph 1

"Any digital representation of value that is not issued or guaranteed by a central bank or a public authority, that is not necessarily attached to a legally accepted currency and does not possess the legal status of currency, but that is accepted by natural or legal persons as a means of exchange and can be transferred, stored, or exchanged electronically."

In other words, EMTs are not considered electronic money but are a type of crypto-asset sharing specific aspects of the legal regime governing electronic money.

On the other hand, PSD2 uses a broad definition of "funds" that includes "electronic money," causing confusion about how to handle EMTs.

The question thus lies in the assimilation of EMTs as funds under PSD2. If these stablecoins were considered funds, they would be subject to the same regulatory requirements as traditional electronic money. However, traditional payment technologies and blockchain technologies differ significantly. Consequently, certain technical requirements of PSD2 pose specific practical obstacles for affected actors, adding an excessive and dual regulatory burden.

4. Impact on Crypto Asset Service Providers (CASPs)

4.1. L'obligation d'obtenir une licence spécifique

First, CASPs could face the obligation to hold a license to offer EMTs to their clients, thereby creating a dual regulatory regime for the same activity. Applying two distinct regulatory regimes for the same service would introduce unnecessary complexity and additional costs. They would need to comply not only with MiCA's requirements but also with the payment institution obligations under PSD. This contradicts the principle of proportionality, which aims to avoid disproportionate burdens relative to the regulatory objectives. Consequently, providing services related to EMTs would become more cumbersome and costly.

They might choose to operate through a Payment Service Provider (PSP) to meet these additional obligations. However, adding an intermediary would make the service less efficient and more costly, negatively impacting the end-user. For example, using an intermediary to transfer EMTs like USDT (Tether), a widely used stablecoin, would increase transaction times and fees for users. CASPs might then be incentivized to offer services on other types of assets, such as ARTs (Asset-Referenced Tokens), to avoid the regulatory complexity associated with EMTs.

Example with USDT (Tether)

Take the example of USDT, a popular stablecoin pegged to the U.S. dollar. If CASPs were required to comply with both MiCA and PSD to offer USDT transfer services, they would face doubled licensing and compliance obligations. This would include segregating client funds from corporate funds and subscribing to additional insurance policies. Ultimately, this would lead to higher fees for users wanting to transfer USDT, as CASPs would pass these extra costs onto users.

4.2. Difficulties accessing traditional payment infrastructures

Access to traditional payment infrastructures is one of the main obstacles for CASPs. Access to a primary banking partner directly involved in these infrastructures is crucial to offer payment services. However, major financial institutions have historically avoided the crypto-assets sector

and, more broadly, Web3, sometimes even restricting their clients' access to services provided by CASPs, including those duly registered.

4.3. The limits of the agent-distributor model for CASPs

The agent-distributor model initially appeared to be a promising potential solution for integrating payment services into the crypto-assets field. In practice, however, it has proven to be, as it stands, hardly viable for several reasons.

Firstly, most, if not all, CASPs are not licensed as payment service providers (PSP) like Electronic Money Institutions (EMI) or Payment Institutions (PI), which is essential to offer payment and electronic money services. Without this accreditation, they cannot act as agents for other CASPs or effectively provide payment services for EMTs.

Secondly, CASPs using the agent model for payment services face several significant limitations. To date, none of the traditional PSPs are registered or approved as CASPs, and they lack the expertise and resources to manage the crypto wallets necessary for blockchain-based EMTs. Furthermore, their operational and regulatory systems are designed solely for traditional banking transactions, preventing them from promptly providing payment services for EMTs or acting as agents for CASPs. Therefore, these PSPs cannot, without significantly altering their systems, provide the same payment services on EMTs. They are thus unable, in the short term, to designate CASPs as agents to allow them to provide payment services on EMTs.

Thirdly, even if they were to develop this expertise, the necessary adjustments to their authorizations and procedures could take several months, and the current French (PACTE Law of May 22, 2019) and European (MiCA) regulatory frameworks do not foresee an agent model for CASPs, further limiting this approach as a solution to the challenges mentioned.

5. Other problematic requirements under PSD2

Among PSD2's requirements, others prove difficult to implement with crypto-assets, as the directive was designed for fiat currency and established, different technologies.

For example (non-exhaustive):

- The rules on the segregation of client funds are challenging to apply as exchange platforms often use shared wallets, unlike traditional banks, which segregate client funds on an individual basis.
- Trading activities conducted by exchange platforms (which, unlike traditional financial markets, mix order execution and custody) require the use of omnibus wallets, where client funds are pooled in the same wallet address.

- Specific obligations regarding the rights and obligations associated with the provision and use of payment services, as well as the implementation of restriction, registration, monitoring, and tracking procedures for access to sensitive payment data, will require very demanding compliance from CASPs under PI/EMI approval.

6. Importance of EMTs for the ecosystem

USDT and other popular EMTs like USDC (USD Coin) and BUSD (Binance USD) are widely used by users and service providers. Each of these stablecoins has its own characteristics and stabilization mechanisms. The use of EMTs varies from one CASP to another, depending on their strategies and the services offered. However, their central role makes them essential elements of the crypto ecosystem, both for CASPs and end-users.

Examples: transfer of EMTs from CASP to CASP, used as privileged trading pairs on exchange platforms (CEX), used in perpetual on-chain contracts (PERP), used in yield farming strategies to generate returns distributed to users, etc.