WORLD FEDERATION OF EXCHANGES

WFE Response to the European Union Commission's Consultation – On an EU Framework for Markets in Crypto-Assets

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Background

We are grateful for the opportunity to respond to the EU Commission's consultation paper *On an EU Framework for Markets in Crypto-Assets*.

The World Federation of Exchanges (WFE) is the global trade association for regulated exchanges and clearing houses. We represent over 250 market-infrastructure providers, spread across the Asia-Pacific region (~37%), EMEA (~43%) and the Americas (~21%).

With extensive experience of developing and enforcing high standards of conduct, WFE members support an orderly, secure, fair and transparent environment for all sorts of investors and companies wishing to raise capital and manage financial risk.

We seek outcomes that maximise financial stability, consumer confidence and economic growth. We also engage with policy makers and regulators in an open, collaborative way, reflecting the central, public role that exchanges and CCPs play in an internationally integrated financial system.

If you have any further questions, or wish to follow-up on our contribution, the WFE remains at your disposal. Please contact:

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Questions

5) Do you agree that the scope of this initiative should be limited to crypto assets (and not be extended to digital assets in general)?

♣ **Yes**

♣ **No**

♣ **Don't know/no opinion**

Please explain your reasoning (if needed).

We believe there could be value in adopting a single EU classification which covers both: digital-assets and also crypto assets, as a subcategory. As detailed below, this should also take the form of guidance which provides clarity and certainty but enables individual jurisdictions the right level of autonomy to properly safeguard and manage the requirements of their local market structure, whilst also enabling regulatory deference in the regulation of digital assets in third country jurisdictions. However, for the purposes of clarity we have made reference to 'crypto assets' rather than 'digital assets' in the responses to the questions of this consultation.

6) In your view, would it be useful to create a classification of crypto-assets at EU level?

- **Yes**
- **No**
- **Don't know/no opinion**

If yes, please indicate the best way to achieve this classification (non legislative guidance, regulatory classification, a combination of both…). Please explain your reasoning.

Yes. Whilst a more universal classification would be welcome in the crypto asset taxonomy, it will be important to consider this in an internationally applicable manner and to have the suitable flexibility within that classification to mould to international classifications as they develop. Providing clarity around classification would be beneficial in helping to build consensus and creating harmony within the member states of the EU, as well as with other jurisdictions globally. Some regulatory bodies have made more progress than others in attempting this and learning can be taken from these experiences.

It is important that definitions should aim to facilitate greater clarity on the types of asset that already fall within the regulatory perimeter and the type of platforms where they are available. The WFE would also advocate the avoidance of detailed 'technical' definitions, which may be too specific in what they capture, when the field of products are evolving and may quickly fall outside of what is defined in technical terms due to these rapid technological advancements. Instead, the definitions should be based on the value of the assets represented/embodied. That is, if security tokens represent a "financial instrument" defined in MiFID II under Annex I, Section C of the MiFID II (1)-(11), then they should be treated as such an instrument under existing regulation, e.g. if the embodied value is a share, then all rules for shares apply, if the embodied value is a commodity, then all rules for commodities apply.

A commonly understood approach, based on existing application of rules and regulations for the financial market would provide much needed legal certainty to reduce regulatory arbitrage, inconsistencies and market fragmentation and to ensure scalability of services. However, such an approach would need to acknowledge and incorporate the flexibility to give the suitable autonomy of individual jurisdictions to apply their own, appropriate, specific regulatory requirements to the regulation of crypto assets, in line with the needs of local markets. Whilst also enabling regulatory deference towards the regulation of crypto assets (and digital assets in general) in third country jurisdictions. This will be key to ensuring that it can be applied in the aforementioned international manner. This could have the potential to enhance the speed to market for innovative products, as market participants and authorities would act within a well-established, more clearly defined, legal framework and with a set of rules which are appropriate for institutional and retail investors.

8) Do you agree that any EU classification of crypto-assets should make a distinction between 'payment tokens', 'investment tokens', 'utility tokens' and 'hybrid tokens'?

- **Yes**
- **No**
- **Don't know/no opinion**

Please explain your reasoning (if needed). If yes, indicate if any further subclassification would be necessary.

Yes, however, it is noticeable that these classifications are different in terminology compared to some jurisdictions who have already sought to establish classifications. It will be important to ensure that the classification and definitions used are the most universal and best understood by the widest audience – both within and beyond the EU.

More broadly, a clear and distinct classification of crypto assets between security-, payment/exchange-, utility- and hybrid-asset is deemed of key importance to determine if a given crypto asset falls under an existing EU regulative framework and for users to align to the existing regulation. It should also be considered as to whether the evolving nature of the crypto asset market, and its associated products, may mean that such classification will need to have suitable flexibility to 'absorb' new innovations or that additional classifications may be needed. For example, clarification of associated forms of payment/exchange tokens may be beneficial given it is an already evolving field, i.e. crypto-currencies, stablecoins, digital bank money and central bank digital currencies. Furthermore, perhaps the most immediately relevant distinction of crypto assets for the exchange industry today is whether or not something is a "security token" and thus subject to securities laws; we believe it would be essential for any framework to be clear about this definition and its distinction from other "investment tokens". Consideration should also be given, when defining the classifications, that it does not give rise to a set of products which actively seek to stand outside the regulatory sphere as this could led to investor protection issues.

14) In your view, would a bespoke regime for crypto assets (that are not currently covered by EU financial services legislation) enable a sustainable crypto asset ecosystem in the EU (that could otherwise not emerge)?

- **Yes**
- **No**
- **Don't know/no opinion Please explain your reasoning (if needed).**

The EU should seek to create an environment which fosters innovation, while preserving financial stability and market integrity. A common framework, in the manner outlined in response to question 6, is beneficial in creating certainty and scalability for new products. Whilst a 'bespoke regime' is discussed, the appropriate application of existing regulations is an important component to that certainty as the "same business, same risks, same rules" principle is necessary for regulation of future technologies/products in order to remain technology neutral, enabling a level playing field. Existing regulation should, naturally, be supplemented where required to address any specific technology related emerging "new" risks. This would provide legal certainty for market participants as they ensure high standards of investor protection and market integrity.

27) In your opinion and beyond market integrity risks (see section III. C. 1. below), what are the main risks in relation to trading platforms of crypto-assets? Please rate each proposal by level of relevance from 1 to 5, 1 standing for "completely irrelevant" and 5 for "highly relevant".

	1	2	3	4	5	No opinion
Absence of accountable entity in the EU						✖
Lack of adequate governance arrangements, including operational resilience and ICT security					✖	
Absence or inadequate segregation of assets held on the behalf of clients (e.g. for 'centralised platforms')						✖
Conflicts of interest arising from other activities				✖		
Absence/inadequate recordkeeping of transactions					✖	
Absence/inadequate complaints or redress procedures are in place			✖			
Bankruptcy of the trading platform			✖			
Lacks of resources to effectively conduct its activities			✖			
Losses of users' crypto-assets through theft or hacking (cyber risks)				✖		
Lack of procedures to ensure fair and orderly trading					✖	
Access to the trading platform is not provided in an undiscriminating way				✖		
Delays in the processing of transactions			✖			
For centralised platforms: Transaction settlement happens in the book of the platform and not necessarily recorded on DLT. In those cases, confirmation that the transfer of ownership is complete lies with the platform only (counterparty risk for investors vis-à-vis the platform)			✖			
Lack of rules, surveillance and enforcement mechanisms to deter potential market abuse					✖	
Other						

Please explain your reasoning (if needed).

The WFE would like to highlight the importance of distinguishing between so-called "crypto asset exchanges" and the regulated, secure and lit markets that established exchanges provide.

Since the emergence and popularity of crypto currencies (Bitcoin, Ethereum, and many more), crypto asset platforms have been referred to as "exchanges", implying that they qualify as such in the traditional sense. This can deceive investors into thinking that such entities are regulated or meet the regulatory standards of traditional

exchanges when they do not (a perception that has unfortunately been falsely perpetuated by some "crypto asset exchanges" in the recent past).

While some crypto asset platforms enforce their own standards, unless they are recognised by regulatory authorities and adhere to a set of acknowledged regulations, they cannot offer the same security to market participants. This includes having an appropriate level or pre – and post-trade transparency. Regulation should ensure that there is no substantial difference between trading against fiat-based products to when trading that of crypto asset based products. The 'same risk, same rule' principle should apply. With consumer protection and market integrity in mind, crypto asset platforms and their users would benefit from greater clarity when navigating regulatory obligations e.g. registration, consumer rights and /protections, licensing, and investor disclosure.

With consumer protection and market integrity also in mind, a clear distinction should be made between these two types of institution through a form of regulatory recognition, in order to avoid deceiving investors and present them with a sense of false security. Crypto asset platforms should only be referred to as "exchanges" where they are compliant with the regulations pertinent to traditional exchanges. If they do not adhere to such standards, they should not use the term "exchange".

This statement applies to question 29, 30, 37 and 38 of the consultation paper, as well as to aspects of other relevant questions.

41) Do you consider it appropriate to extend the existing 'virtual currency' definition in the EU AML/CFT legal framework in order to align it with a broader definition (as the one provided by the FATF or as the definition of 'cryptoassets' that could be used in a potential bespoke regulation on cryptoassets)?

The WFE would recommend any appropriate opportunity to align definitions with those operated by international standard setting bodies, such as the FATF. Harmonising language and definitions are core to the delivery of better regulatory outcomes and enabling a safe yet efficient global trading environment.

42) Beyond fiat-to-crypto exchanges and wallet providers that are currently covered by the EU AML/CFT framework, are there crypto-asset services that should also be added to the EU AML/CFT legal framework obligations? If any, please describe the possible risks to tackle.

Any crypto asset platform purporting to operate as an 'exchange' or able to provide trading venue or FMI services, especially those available to retail investors, should conform and abide by the AML/CFT regulatory requirements imposed on traditional market infrastructure. To remove or dilute any such requirements would appear to run contrary to the delivery of safe and efficient markets for consumers. This would also potentially reduce the regulatory burden on such platforms and create unbalanced competitive marketplace for traditional market infrastructure to operate in. The investment made by established market infrastructure is to ensure that high standards are embedded in the services they provide which, in turn, ensure the economies they serve are well protected and insulated from the risk associated with lax AML/CFT regulatory requirements.

43) If a bespoke framework on crypto-assets is needed, do you consider that all crypto-asset service providers covered by this potential framework should become ‘obliged entities’ under the EU AML/CFT framework?

- **Yes**
- **No**
- **Don't know/no opinion**

Yes.

45) Do you consider that these requirements should be introduced in the EU AML/CFT legal framework with additional details on their practical implementation?

- **Yes**
- **No**
- **Don't know/no opinion**

Yes, as outlined in response to question 42.

51) In your opinion, how should the crypto-assets issued in third countries and that would not comply with EU requirements be treated? Please rate each proposal from 1 to 5, 1 standing for "not relevant factor" and 5 for "very relevant factor".

	1	2	3	4	5	No opinion
Those crypto-assets should be banned	✖					
Those crypto-assets should be still accessible to EU consumers/investors					✖	
Those crypto-assets should be still accessible to EU consumers/investors but accompanied by a warning that they do not necessarily comply with EU rules						✖
Other						

Please explain your reasoning (if needed).

In order to enable cross-border trade, any approach would need to acknowledge and incorporate the flexibility to give suitable autonomy to individual jurisdictions to apply their own, appropriate, specific regulatory requirements to the regulation of crypto assets, in line with the needs of local markets. Whilst, also enabling regulatory deference towards the regulation of crypto assets (and digital assets in general) in third country jurisdictions. This will be key to ensuring that it can be applied in an international manner (outlined in response to question 6).

52) Which, if any, crypto-asset service providers included in Section III. B do you think should be subject to supervisory coordination or supervision by the European Authorities (in cooperation with the ESCB where relevant)? Please explain your reasoning (if needed).

Any crypto asset service provider which purports to operate/provide the services of market infrastructure, and classifies itself as an exchange, should be subject to the supervision of the jurisdiction's regulatory authorities. As outlined in response to question 27.

55) Do you think that DLT could be used to introduce efficiencies or other benefits in the trading, post-trade or asset management areas?

Completely agree	
Rather agree	✖
Neutral	
Rather disagree	
Completely disagree	
Don't know / No opinion	

Please explain your reasoning (if needed). If you agree, please indicate the specific areas where, in your opinion, the technology could afford most efficiencies when compared to the legacy system. [Insert text box]

The WFE strongly supports the nurturing of innovation and technology which benefits consumers and provides enhanced, safer and more efficient marketplaces. The use of DLT is something that many of our members (in the market infrastructure sector) are exploring to achieve those aims. However, it should be readily understood that such technologies cannot replace certain aspects of what established exchanges and FMI provide – that of addressing/managing risk. At its heart, DLT is no more than a (streamlined) means of record keeping. As such it supports but does not replace the core functions performed by exchanges, creating and operating a market and acting as a source of valuable data. (Nor does it replace the clearing function, which consists of imposing a discipline on market participants who maintain open credit exposures to each other). We should equally not lose sight of the fact that a transition from legacy to new infrastructure requires a concerted effort not only from the operator but from the users of such services to ensure continued integration into their business flows.

Where DLT is being adopted it should be considered within the existing regulatory framework, to the extent that is practicable, and appropriate deference should be provided by the EU to third-countries' approach to the regulation of DLT.

56) Do you think that the use of DLT for the trading and post-trading of financial instruments poses more financial stability risks when compared to the traditional trading and post-trade architecture?

Completely agree	
Rather agree	
Neutral	✖
Rather disagree	
Completely disagree	
Don't know / No opinion	

Please explain your reasoning (if needed).

The appropriate use of such technologies can potentially offer enhancements for consumers and for the delivery of safe and efficient marketplaces. However, such technologies should be delivered with experienced oversight from both the industry seeking to use it and from the supervisory authorities charged with regulating its use. As with all new technologies, to enable its use to progress the industry, a balance must be found between unnecessarily stifling innovation with draconian rules and having too loose a regulatory environment without proper controls. Inappropriate use or inexperienced oversight might result in negative, unforeseen, consequences.

However, the application of such technologies must also consider what it can and what it cannot do. It cannot yet replace the current services provided by CCPs as it does not have the same core objectives and criteria of oversight because it has not been designed nor capable of replicating those functions. Confusion or misplaced faith in the ability of technology – and, by extension, those ultimately responsible for its development and maintenance – to replace such functions could inadvertently have a much greater impact on financial stability.

We note a potential risk where unregulated firms, who offer direct services to investors, lead the development/implementation of DLT solutions related to core market functions. A lack of awareness of the regulatory environment and different risk culture may result in negative consequences for investor protection, and secure and orderly markets.

57) Do you consider that DLT will significantly impact the role and operation of trading venues and post-trade financial market infrastructures (CCPs, CSDs) in the future (5/10 years' time)? Please explain your reasoning.

As discussed in questions 55 and 56, the use of DLT and other technologies is being pursued by the WFE's membership to harness the benefits and efficiencies that can be derived for their consumers and the marketplace. Whilst it is difficult to speculate about the future of technology in the age of rapid advancements, the care and sensitivity that needs to be applied to the financial services industry should result in very careful application and supervision of new systems operating in market infrastructures or those which claim to provide those services. In order to ensure that orderly and managed integration established and experienced businesses who work with the regulatory authorities are best placed to oversee any introduction of DLT in the operation of trading venues and post-trade financial market infrastructures. The ability to coordinate multiple stakeholders to safely and successfully navigate large, disruptive shifts in the technology landscape is, indeed, a strength of the 'traditional' exchange industry (e.g. the electronification of order books).

However, as highlighted in the recent OECD report on the tokenisation of assets[1], there are still a number of issues to overcome in the embedding of DLT in such services. Technology must also be readily understood as to what service it provides and how well it can scale and be safely implemented. Distributed ledger technology (DLT) enables the decentralisation of record-keeping. It does so by removing the need for a central ledger in which to record financial transactions[2]. It is not purposed to replace the role of CCPs (see response to question 103). DLT may be able to reduce operating costs and speed up settlement. But that does require integration and alignment with a number of other long-established processes. Even then, it seems unfeasible – and more importantly undesirable – to take trusted third parties (ie, exchanges and CCPs) out of the equation.

[1] OECD (2020), The Tokenisation of Assets and Potential Implications for Financial Markets, OECD Blockchain Policy Series, www.oecd.org/finance/The-Tokenisation-of-Assets-and-PotentialImplications-for-Financial-Markets.htm.

[2]Decentralised financial technologies Report on financial stability, regulatory and governance implications, FSB, June 2019, https://www.fsb.org/wp-content/uploads/P060619.pdf

58) Do you agree that a gradual regulatory approach in the areas of trading, post trading and asset management concerning security tokens (e.g. provide regulatory guidance or legal clarification first regarding permissioned centralised solutions) would be appropriate?

Completely agree	
Rather agree	
Neutral	✖
Rather disagree	
Completely disagree	
Don't know / No opinion	

Please explain your reasoning (if needed).

The WFE believes the scope of existing regulations should be sufficient to extend to most potential DLT use cases (which are typically new technologies as opposed to new activities). Legislation, rules and supervisory practices should only be adapted if strictly required and avoid conferring undue advantage to one technology over another or inadvertently limiting competition by unnecessarily increasing barriers to entry.

We consider it important innovation should be market driven and needs to take place in a safe and controlled environment in which participants can have confidence. Any regulatory approach should encourage innovation whilst ensuring appropriate investor protection, security in the system and stability of the financial markets.

Authorities should continue to proactively engage with industry to identify the nature of the application, understand the technology behind it, and ensure an appropriate regulatory framework (if existing frameworks are not deemed appropriate).

As previously highlighted, we note a potential risk where unregulated firms, who offer direct services to investors, lead the development/implementation of DLT solutions related to core market functions. A lack of awareness of the regulatory environment and different risk culture may result in negative consequences for investor protection, and secure and orderly markets.

59) Do you think that the absence of a common approach on when a security token constitutes a financial instrument is an impediment to the effective development of security tokens?

Completely agree	✖
Rather agree	
Neutral	
Rather disagree	
Completely disagree	
Don't know / No opinion	

Please explain your reasoning (if needed). [Insert text box]

The EU should seek to create an environment which fosters innovation, while preserving financial stability and market integrity. A common framework is beneficial in creating certainty for new products. The application of existing regulations is an important component to that certainty, and we believe that where security tokens meet the definition of a specified investment they may fall within the regulatory perimeter of the supervisory authority.

Securities tokens grant their holders rights similar to (or purported to be similar to) that of traditional securities and in some jurisdictions may be considered equal to those and therefore may be regulated as such.

Additionally, security tokens derive their value not from themselves but from an underlying element which is coordinated though a specified issuer and presents the holder with some form of ownership (hence the aforementioned rights). Security tokens are therefore just as centralised as traditional investment instruments.

For a security token to be a transferable security under MiFID, it must be “negotiable” on the capital markets. We believe that this requirement of MiFID is beneficial in clarifying the transformation of a new element of capital market structures into a regulated environment. Requiring that shares be negotiable in order to consider them specified investment, ensures that the trading of innovative (and so by definition previously unknown) instruments are kept in regulated and supervised environments. This can help to safeguard the integrity of the market as new instruments develop.

A common approach helps to deliver these positive outcomes.

60) If you consider that this is an impediment, what would be the best remedies according to you? Please rate each proposal from 1 to 5, 1 standing for "not relevant factor" and 5 for "very relevant factor".

	1	2	3	4	5	No opinion
Harmonise the definition of certain types of financial instruments in the EU					✖	
Provide a definition of a security token at EU level					✖	
Provide guidance at EU level on the main criteria that should be taken into consideration while qualifying a crypto-asset as security token					✖	
Other						

Please explain your reasoning (if needed).

Any definition or approach should be mindful of any international efforts to harmonise the definition and have suitable flexibility to adhere to those global definitions as they come into play. With global alignment in mind, moving to a definition at EU level, under the reasoning applied in question 59, would be beneficial to the move towards a more harmonised approach.

61) How should financial regulators deal with hybrid cases where tokens display investment-type features combined with other features (utility-type or payment type characteristics)? Please rate each proposal from 1 to 5, 1 standing for "not relevant factor" and 5 for "very relevant factor".

	1	2	3	4	5	No opinion
Hybrid tokens should qualify as financial instruments/security tokens					✖	
Hybrid tokens should qualify as unregulated crypto-assets (i.e. like those considered in section III. of the public consultation document)						
The assessment should be done on a case-by-case basis (with guidance at EU level)						
Other						

Where there is uncertainty, where tokens display investment-type features combined with other features, hybrid tokens should be subject to "stricter" regulations (e.g. dealt with under securities law) and it should be clarified if certain features are incompatible.

66) Would you see any particular issues (legal, operational) in applying trading venue definitions and requirements related to the operation and authorisation of such venues to a DLT environment which should be addressed? Please explain your reasoning (if needed).

No, in the sense that such requirements should be applied if they are performing the same function. More broadly, this was outlined in IOSCO's 2020 report "Issues, Risks and Regulatory Considerations Relating to Crypto-Asset Trading Platforms (CTPs)", in which it is referred to that many of the issues related to the regulation of CTPs are common to traditional securities trading venues but may be heightened by the business models used by CTPs. Where a regulatory authority has determined that a crypto asset is a security and falls within its remit, the basic principles or objectives of securities regulation should apply. The report highlighted a number of areas where CTPs operating DLT technology required important regulatory considerations in this context.

67) Do you think that current scope of investor protection rules (such as information documents and the suitability assessment) are appropriate for security tokens? Please explain your reasoning (if needed).

Yes, security tokens may meet the definition of a specified investment and fall within the regulatory perimeter of the supervisory authority. Where that is the case, regulatory rules should apply equally. Application of the rules and the associated necessary investments protections and burdens have been developed to ensure market and consumer protections. Any MiFID Review may want to consider the specific risks attached to crypto assets and give consideration to particular elements such as the need for additional IT related requirements to protect consumers and market integrity (inclusive of the DLT network).

71) Would you see any particular issue (legal, operational) in applying these requirements to security tokens which should be addressed? Please explain your reasoning (if needed).

No. As outlined in response to question 67 answers, security tokens may meet the definition of a specified investment and therefore fall within the regulatory perimeter of the supervisory authority. Where this is the case, regulatory rules should apply equally. Application of the rules and the associated necessary investments protections and burdens have been developed to ensure market and consumer protections.

72) Would you see any particular issue (legal, operational) in applying these requirements to security tokens which should be addressed? Please explain your reasoning (if needed).

Established trading venues have developed appropriate rules and principles in accordance with their high standards and regulatory requirements. A benefit of enabling established venues to trade security tokens is that by their nature these established venues will have the appropriate rules in place. For crypto asset platforms providers, it is important for the purposes of market and consumer protection to enforce rules which bring them to the standards adhered to by established venues.

73) What are the risks and benefits of allowing direct access to trading venues to a broader base of clients? Please explain your reasoning (if needed).

The standards and existing regulatory requirements applied to established market infrastructure under MiFID, should equally be applied to crypto asset platforms where they use the term “exchange” to refer to the services they offer. This is important in ensuring a level playing field and achieving the associated aims of consumer protection.

However, it is important to recognise an important distinction regarding the role of derivative products and derivatives exchanges which widely offer risk management tools for underlying markets that may not be regulated, nor are traded on regulated venues. This can be witnessed with other asset classes, such as energy, agriculture or metals. An approach that ‘curtails’ the ability for derivative exchanges to offer such products, may inadvertently, have a damaging effect on the real economy, stifle innovation and inhibit the development of emerging market economies.

Any approach would also need to acknowledge and incorporate the flexibility to give suitable autonomy of individual jurisdictions to apply their own, appropriate, specific regulatory requirements to the regulation of crypto assets, in line with the needs of local markets while also enabling regulatory deference towards the regulation of crypto assets (and digital assets in general) in third country jurisdictions. This will be key to ensuring that it can be applied in an international manner (outlined in response to question 6).

74) Do you think these pre- and post-transparency requirements are appropriate for security tokens?

Option	
Completely agree	✖
Rather agree	
Neutral	
Rather disagree	
Completely disagree	
Don't know / No opinion	

Please explain your reasoning (if needed).

If security token meets the definition of a specified investment and therefore fall within the regulatory perimeter of the supervisory authority, then those regulations should be applied fairly and evenly. The "same business, same risks, same rules" principle is necessary for regulation of future technologies/products in order to remain technology neutral. This would include the application of reporting through an Approved Publication Arrangement (APA), e.g. the identifier of the financial instrument, the price, volume and the time of the transaction and the code for the trading venue.

That said, again, it is important to observe that it is not the case that crypto assets (as with all cash markets) must be regulated financial instruments, or traded on a trading venue in order for derivative products to be based on those assets.

75) Would you see any particular issue (legal, operational) in applying these requirements to security tokens which should be addressed (e.g. in terms of availability of data or computation of thresholds)? Please explain your reasoning (if needed).

If security token meets the definition of a specified investment and therefore falls within the regulatory perimeter of the supervisory authority, then those regulations should be applied fairly and evenly. The "same business, same risks, same rules" principle is necessary for regulation of future technologies/products in order to remain technology neutral and ensure a level playing field, whilst providing consumer protections.

76) Would you see any particular issue (legal, operational) in applying these requirement to security tokens which should be addressed? Please explain your reasoning (if needed).

As outlined in response to question 75, if a security token meets the definition of a specified investment and therefore falls within the regulatory perimeter of the supervisory authority, then those regulations should be applied fairly and evenly. The "same business, same risks, same rules" principle is necessary for regulation of future technologies/products in order to remain technology neutral and ensure a level playing field.

82) Do you consider that different or additional exemptions should apply to security tokens other than the ones laid down in Article 1(4) and Article 1(5) of PR?

Completely agree	
Rather agree	
Neutral	
Rather disagree	
Completely disagree	✖
Don't know / No opinion	

Please explain your reasoning (if needed).

If security token meets the definition of a specified investment and therefore falls within the regulatory perimeter of the supervisory authority, then those regulations should be applied fairly and evenly. Further, a common framework is beneficial in creating certainty for new products. The application of existing regulations is an important component to that certainty and a balanced regulatory environment. If there is an obligation under existing regulation to publish a prospectus for a security token, all existing rules and exemptions should apply. Additionally, whilst avoiding undue burdens, it might be useful to detail in the prospectus about the technological features of the assets. If security tokens are treated as securities, they must be able to be identified via an ISIN or appropriate global identifiers. This would also help to process digital securities in established IT systems.

101) Do you think that security tokens are suitable for central clearing?

Completely appropriate	
Rather appropriate	
Neutral	
Rather inappropriate	
Completely inappropriate	
Don't know / No opinion	

Please explain your reasoning (if needed).

In theory, there is no reason in principle why some security tokens could not be centrally cleared, bringing the benefits of multilateral netting and netting between different asset-classes and collateral and default management processes which cannot yet be directly replaced by DLT today. Please note, however, that the process of clearing (as distinct from settlement) is really about credit exposure reduction and mitigation, and therefore raises issues related to the liquidity and ability to assess the risk of the instrument in question. (Settlement – the actual exchange of cash or other assets in return for a specific financial instrument – is a different and more purely operational matter.) The ability of a CCP to service any market should in principle be a function of its ability to effectively manage risk exposure and prepare for the possible failure of market participants. Should one of those participants fail, then all attention will turn on how well the CCP can remedy the situation, which may mean exposure to a rapidly changing asset price, the risk of which the CCP would assess prior to the default event and require market participants to mitigate. This in turn means the CCP has to be able to model that risk to a regulatory approved statistical confidence level.

The distinction outlined above, between clearing and settlement, becomes more important when one moves beyond the (normally relatively short) timeline of the securities horizon and into the handling of term contracts, i.e., repo and derivatives. Conversely, if time to settlement of tokens is reduced to zero or thereabouts (perhaps through the use of DLT), then this risk may be lessened. As discussed elsewhere in our response, however, it may be difficult to move the whole market simultaneously to 'T+0', given the many technological and logistical challenges of aligning other related processes, although it is worthwhile recalling that certain products already process within a T+0 environment even within legacy technology. It may also be somewhat misleading to characterise 'T+0' as a necessarily desirable outcome for securities settlement (whether in tokenised form or not), since instant settlement of trades could have a significant dampening effect on the viability of economic activities (such as market-making and liquidity provision more generally) that help make such markets liquid and attractive for investing in the first place.

102) Would you see any particular issue (legal, operational, technical) with applying the current rules in a DLT environment? Please rate each proposal from 1 to 5, 1 standing for "not a concern" and 5 for "strong concern".

	1	2	3	4	5	No opinion
Rules on margin requirements, collateral requirements and requirements regarding the CCP's investment policy						
Rules on settlement						
Organisational requirements for CCPs and for TRs						
Rules on segregation and portability of clearing members' and clients' assets and positions						
Rules on requirements for participation						
Reporting requirements						
Other (including other provisions of EMIR, national rules applying the EU acquis, supervisory practices, interpretation, applications…)						

Please explain your reasoning (if needed).

Whilst we envisage efficiencies to processes being borne out by the use of such technology, we

do not see the DLT environment, per se, as relevant to the question of clearing. DLT records settlement. (Please see our answer to question 101 for more on this.)

103) Would you see the need to clarify that DLT solutions including permissioned blockchain can be used within CCPs or TRs?

The type of technology used to record or effect settlement would not, prima facie, seem to us to be a matter for legislation. The exception to this may be related to the fact that the key test would appear to be whether settlement finality can be supported via DLT.

104) Would you see any particular issue with applying the current rules to derivatives the underlying of which are crypto assets, in particular considering their suitability for central clearing? Please explain your reasoning (if needed).

As a general principle, we believe it is preferable to see crypto assets within a well-regulated and transparently organised infrastructure environment (whether exchange or CCP) rather than outside it. But, as outlined in our response to question 101, the question as to whether central clearing is a suitable arrangement for derivatives on *any* given asset – whether crypto, commodity, financial asset, currency or anything else – will require a CCP to make a carefully considered judgement as to the liquidity and ability to assess the risk of the underlying asset. Central clearing brings important benefits, notably in terms of netting down open positions (including long-dated positions in derivatives). It is not consistent with that reality to adopt blanket judgements about whether an asset of particular legal or operational form lends itself to central clearing.

108) Do you think that the EU legislation should provide for more regulatory flexibility for stakeholders to develop trading and post-trading solutions using for example permissionless blockchain and decentralised platforms?

♣ **Yes**

♣ **No**

♣ **Don't know/no opinion**

If yes, please explain the regulatory approach that you favour. Please explain your reasoning (if needed).

The EU should seek to create an environment which fosters innovation, while preserving financial stability and market integrity. A common legal framework is beneficial in creating legal certainty for new products. The application of existing regulations is an important component to that certainty. Permissionless and decentralised platforms are considered as having a number of security related concerns which would require careful monitoring coupled with the issues of data protection which could if abused lead to market manipulation. The "same business, same risks, same rules" principle is necessary for regulation of future technologies/products in order to remain technology neutral.

110) Do you think that the regulatory separation of trading and post-trading activities might prevent the development of alternative business models based on DLT that could more efficiently manage the trade life cycle?

♣ **Yes**

♣ **No**

♣ **Don't know/no opinion**

If yes, please identify the issues that should be addressed at EU level and the approach to address them. Please explain your reasoning (if needed).

Whilst advancements have been made in the trade life cycle through technology, there are still a number of questions over how the application of this technology relates to the rest of the system, such as the payment system. To create new forms of regulation to accommodate a relatively untested approach may create a form of arbitrage, especially when the technology is unproven and evolving.