Introduction and legal basis

On 18 and 30 November 2020 the European Central Bank (ECB) received requests from the Council and the European Parliament, respectively, for an opinion on a proposal for a regulation on a pilot regime for market infrastructures based on distributed ledger technology (hereinafter the ‘proposed regulation’).

The ECB’s competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union, as the proposed regulation contains provisions falling within the ECB’s fields of competence, in particular, the definition and implementation of monetary policy, the promotion of the smooth operation of payment systems, contribution to the smooth conduct of policies pursued by competent authorities relating to the stability of the financial system, and the ECB’s tasks concerning the prudential supervision of credit institutions pursuant to Article 127(2), first and fourth indents, Article 127(5) and Article 127(6) of the Treaty. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. General observations

1.1. The ECB welcomes the proposed regulation, which aims to enable investment firms, market operators and central securities depositories (CSDs) to operate market infrastructures based on distributed ledger technology (DLT), either as a DLT multilateral trading facility (hereinafter referred to as a ‘DLT MTF’) or a DLT securities settlement system (SSS) (hereinafter referred to as a ‘DLT SSS’ or together with DLT MTFs as ‘DLT market infrastructures’).

1.2. The ECB welcomes the limitations that the proposed regulation brings, both in terms of asset classes and market size, as regards the DLT transferable securities (T) available for registration, trading and settlement via DLT MTFs and DLT SSSs while facilitating the mitigation of potential risks associated with the use of DLT. Nevertheless, it could be further considered whether to extend the asset classes, while maintaining the thresholds, to include sovereign bonds. That said, the ECB emphasises that its opinion is predicated on the understanding that the specific thresholds set out in the proposed regulation (T) are preserved, as any increase in these thresholds might pose risks to the level playing field between incumbent and DLT market infrastructures and possibly also to the stability of the financial system. Moreover, the ECB believes that, bearing in mind the level of capital markets’ development in some EU Member States, it would be advisable to consider providing the national competent authorities with an option to lower the relevant thresholds. Consequently, the ECB wishes to be reconsulted on the proposed regulation if there is any material alteration to the thresholds. In addition, it should be ensured these thresholds are not circumvented, as this would undermine their effectiveness. For instance, it should not be
possible for an issuer to divide the issuance of bonds into two (or more) tranches to be issued via a single DLT market infrastructure. In this context, imposing obligations only on operators of DLT market infrastructures may prove ineffective if not complemented by obligations on the issuers of bonds. Furthermore, an additional threshold, set at the level of a DLT market infrastructure on the basis of settled value, could be contemplated, as this is one of the relevant indicators used in assessing the systemic importance of a settlement infrastructure. Finally, the ECB understands that, under the proposed regulation, meeting the thresholds is not a sufficient condition to be exempted from Union legislative requirements. Even when the thresholds are fully met, operators of DLT market infrastructures can only be exempted on a case-by-case basis by the relevant competent authorities also subject to financial stability considerations.

1.3. Under the proposed regime, operators of DLT MTFs may provide services in addition to those provided under Directive 2014/65/EU of the European Parliament and of the Council (1) (hereinafter referred to as ‘MiFID II’); namely, they may provide core CSD services (2). The provision of such additional services would entail new and additional risks for their participants that need to be catered for by the proposed regulation. However, the additional requirements set out in the proposed regulation appear rather limited. Therefore, the proposed regulation does not seem to ensure a level playing field between DLT MTFs and DLT SSSs as well as between these DLT market infrastructures and CSDs operating SSSs based on traditional technology as these provide similar services in competition with one another. In other words, the proposed regulation does not follow the principle of ‘same business, same risks, same rules’. Furthermore, while the proposed regulation envisages that an operator of an MTF can settle DLT transferable securities, the opposite possibility of a CSD operating a DLT SSS also operating an MTF should be explored as well. This consideration stems from the fact that, as acknowledged in the recitals to the proposed regulation, the use of DLT, with all transactions recorded in a decentralised ledger, can condense trading and settlement to nearly real-time and could enable the merger of trading and post-trading activities.

1.4. In addition, as regards e-money tokens that may be used for the settlement of DLT transferable securities transactions, the proposed regulation does not seem to respect the principle of technological neutrality. Specifically, while e-money tokens may be issued also based on a technology other than DLT (3), the infrastructures covered under the proposed regulation may be based on DLT only.

1.5. Finally, the ECB, while welcoming the aim of the proposed regulation to support innovation, wishes to highlight a potential shortcoming with regard to the envisaged exemption from the application of the provisions on access set out in Regulation (EU) No 909/2014 (hereinafter referred to as the ‘CSD Regulation’) (4). The ECB believes that such an exemption, if granted in a wide manner by the national competent authorities across the Union, may hamper the CSD Regulation’s aim of harmonising and enhancing the efficiency of cross-border settlement within the Union. Furthermore, the ECB believes that such exemption has the potential to affect interoperability among SSSs, which could ultimately lead to increased fragmentation of liquidity.

2. Monetary policy aspects

2.1. From a monetary policy standpoint, securities transactions are of critical importance for the functioning of the money market and for the conduct of open market operations. In this respect, DLT as an innovative technology to be applied in SSSs to potentially facilitate more efficient execution of securities transactions could bring about opportunities as well as risks. From a monetary policy standpoint, the ability of market participants to efficiently

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(4) See Articles 50 and 53 of the CSD Regulation.
transfer securities is of key importance. Therefore, over the long-term public policy will have to carefully evaluate how this new technology is applied in the existing securities settlement ecosystem and/or whether and how it potentially affects existing arrangements to settle securities.

2.2. In principle, a proliferation of different non-interoperable infrastructures available for securities transactions could lead to fragmentation in collateral and liquidity pools, with implications for monetary policy transmission through its potential effect on collateral availability, collateral valuation and price formation in the market. However, the realisation of such risks would depend on the specific features of the different settlement infrastructures and their functionality in terms of allowing participants to access their collateral on a timely basis.

2.3. In addition, regarding access to central bank liquidity for settlement, the Eurosystem currently supports settlement in central bank money for securities transactions via TARGET2-Securities (T2S). Access by CSDs to T2S is subject to a positive assessment against the eligibility criteria and conditions under the applicable ECB Guidelines (\(^{14}\)). Where no access to central bank money is available to participants in DLT SSSs then commercial bank money, commercial bank money in tokenised form and/or e-money tokens could be used to settle securities transactions. If the proliferation of such DLT SSSs led to a significant increase in the use of commercial bank money or e-money tokens to settle securities transactions, the effects for monetary policy transmission would have to be thoroughly analysed.

3. **Oversight and systemic/financial stability aspects**

3.1. **Role of the ESCB in the area of securities settlement**

3.1.1. Pursuant to the fourth indent of Article 127(2) of the Treaty, as mirrored in Article 3.1 of the Statute of the European System of Central Banks and the European Central Bank (hereinafter referred to as the 'Statute'), one of the basic tasks to be carried out through the ESCB is ‘to promote the smooth operation of payment systems.’ To further the performance of this basic task, ‘the ECB and national central banks may provide facilities, and the ECB may make regulations, to ensure efficient and sound clearing and payments systems within the Union and with other countries’ (\(^{14}\)).

3.1.2. CSDs are financial market infrastructures (FMIs) that are strictly regulated and supervised by different authorities pursuant to the CSD Regulation, which sets out requirements on the settlement of financial instruments as well as rules on the organisation and conduct of CSDs. Furthermore, CSDs must take note of the Committee on Payment and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO) Guidance on cyber resilience (\(^{13}\)), for which detailed implementation guidance has been developed in the Eurosystem Cyber Resilience Oversight Expectations for FMIs (\(^{12}\)), which is addressed to all FMIs. In addition to the supervisory competences entrusted to national competent authorities (NCAs) under the CSD Regulation, the members of the ESCB act as ‘relevant authorities’, in their capacity as overseers of SSSs operated by CSDs, as central banks issuing the most relevant currencies in which settlement takes place and as central banks in whose books the cash leg of transactions is settled (\(^{10}\)). In this regard, recital 8 of the CSD Regulation states that the Regulation should apply without prejudice to the responsibilities of the ECB and the national central banks (NCBs) to ensure efficient and sound clearing systems and payment systems within the Union and other countries. It further states that the CSD Regulation should not prevent the members of the ESCB from accessing information relevant to the performance of their duties (\(^{11}\)), including the oversight of CSDs and other FMIs (\(^{12}\)).

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\(^{13}\) See Article 22 of the Statute.


\(^{11}\) Available on the ECB’s website at www.ecb.europa.eu.

\(^{10}\) See Article 12 of the CSD Regulation.

\(^{12}\) See also Article 13 and Articles 17(4) and 22(6) of the CSD Regulation.

3.1.3. In addition, the members of the ESCB often act as settlement agents for the cash leg of securities transactions and the Eurosystem offers settlement services via T2S (\textsuperscript{\textdegree}) to CSDs (hereinafter referred to as ‘T2S participants’). By means of T2S the Eurosystem provides a single, neutral and borderless settlement service for securities transactions on a delivery versus payment basis in central bank money to euro area and non-euro area CSDs and central banks. The Eurosystem’s oversight of T2S is related to its mandate to ensure efficient and sound clearing and payment systems, while competent and relevant authorities of CSDs aim to ensure their smooth functioning, the safety and efficiency of settlement and the proper functioning of financial markets in their respective jurisdictions.

3.1.4. The proposed regulation sets out a series of exemptions from requirements, obligations and definitions (\textsuperscript{\textdegree}) under the CSD Regulation and Directive \textsuperscript{\textdegree}98/26/EC of the European Parliament and of the Council (hereinafter referred to as the ‘Settlement Finality Directive’) \textsuperscript{\textdegree} that CSDs may request when seeking permission to operate DLT SSSs \textsuperscript{\textdegree}. Such exemptions may be granted by the competent authority following an assessment procedure that does not envisage the involvement of the relevant authorities under the CSD Regulation \textsuperscript{\textdegree}, including, specifically, the members of the ESCB. In particular, the proposed regulation envisages no role for the relevant authorities in the procedure for granting a permission, an exemption or the modification of an existing permission or exemption. The same holds true for the procedure for withdrawing a permission or exemption granted to a CSD operating a DLT SSS \textsuperscript{\textdegree}. In the ECB’s view, the involvement of the relevant authorities in these assessment processes is needed in order to ensure the proper exercise by the relevant authorities of their competences under the CSD Regulation. Hence, the proposed regulation should cater for the involvement of the relevant authorities in the assessment processes referred to in order to properly reflect the allocation of competencies envisaged by the CSD Regulation. Furthermore, the involvement of the relevant authorities should not be confined to CSDs, but extended to cover the operators of DLT MTFs that intend to provide core CSD services. The reason for this is that the competences of the relevant authorities relate to the services regardless of the provider of the services or the technology employed.

3.1.5. Finally, under the CSD Regulation, various provisions of the CSD Regulation, including the requirement to report to competent authorities, do not apply to the members of the ESCB in relation to any CSD which the ESCB central banks directly manage under their own responsibility, \(\textsuperscript{\textdegree}\). Under the proposed regulation, a CSD operating a DLT SSS is subject to the requirements applicable to a CSD under the CSD Regulation, except if such a CSD has sought specific exemptions or permissions from the competent authority \(\textsuperscript{\textdegree}\). Taken together, these provisions mean that a CSD operated by an ESCB central bank which operates a DLT SSS is not required to seek specific exemptions or permissions from a competent authority, since such CSDs are not required to report to competent authorities, and are subject to a limited set of requirements under the CSD Regulation. For the sake of legal certainty, it would be helpful to expressly clarify in the recitals of the proposed regulation that the CSDs operated by ESCB central banks are exempt from the provisions of the proposed regulation concerning the process of granting exemptions and withdrawing permissions \(\textsuperscript{\textdegree}\). In practice, this would imply that ESCB central banks would take advantage of the exemptions envisaged under the proposed regulation based on their own risk analysis.

3.2. Participation of natural persons in DLT market infrastructures

The proposed regulation \(\textsuperscript{\textdegree}\) provides for the possibility for a CSD operating a DLT SSS (as well as for operators of DLT MTFs) to admit as participants natural persons as well as legal persons other than those referred to in the CSD Regulation \(\textsuperscript{\textdegree}\). The proposed conditions for the admission of such persons as participants are rather general. In


\(\textsuperscript{\textdegree}\) See Article 5 of the proposed regulation.


\(\textsuperscript{\textdegree}\) See Article 8(2)(g) of the proposed regulation.

\(\textsuperscript{\textdegree}\) See Articles 10 and 12 of the CSD Regulation.

\(\textsuperscript{\textdegree}\) See Article 8(6) and (7) of the proposed regulation.

\(\textsuperscript{\textdegree}\) See Article 1(4) of the CSD Regulation. Such CSD must have access to the funds of the ESCB central bank and must not be a separate entity.

\(\textsuperscript{\textdegree}\) See Article 5 of the proposed regulation.

\(\textsuperscript{\textdegree}\) See Articles 7 and 8 of the proposed regulation.

\(\textsuperscript{\textdegree}\) See Article 4 and Article 5(4) of the proposed regulation and Article 2(19) of the CSD Regulation.

\(\textsuperscript{\textdegree}\) However, at the same time, the proposed regulation does not provide any exemption from the provisions of Article 33(1) of the CSD Regulation, which refers to certain legal persons as participants of a CSD.
this respect, the regulatory technical standards supplementing the CSD Regulation (\(^9\)) detail legal, financial and operational risks that a CSD must assess when analysing a request for participation. It is unclear how those risks will be assessed where a natural person applies for CSD participation (\(^{10}\)). In this case, where such risks are not properly taken into account, concerns may arise as to how a level playing field can be ensured between traditional and DLT SSSs and regarding the risks that such participants may pose, either to the CSD itself or to its other participants. Similarly, it is unclear which MiFID II requirements applicable to investment firms participating in MTFs (e.g. those related to the use of algorithmic trading) would also be applicable to natural persons participating in DLT MTFs. It may be impossible for some of the requirements on investor protection under MiFID II and Regulation (EU) No 600/2014 of the European Parliament and of the Council (\(^{11}\)) to apply (\(^{12}\)). If there were no intermediation by investment firms, then retail investors could invest in DLT transferable securities that may be unsuitable or inappropriate for them. Furthermore, there is a difference, unsatisfactory in terms of a level playing field, between the requirements applicable to DLT SSSs and DLT MTFs in terms of the maximum period for which natural persons can be admitted as participants in these market infrastructures (\(^{13}\)).

3.3. Settlement of payments in DLT market infrastructures

3.3.1. The proposed regulation envisages that payments may be settled in DLT market infrastructures through three means. First, the settlement of payments may be carried out through central bank money, where practicable and available. Second, where settlement through central bank money is not practicable and available, payments may be settled through commercial bank money, including commercial bank money in a token-based form. The ECB understands that such commercial bank money in a token-based form, also referred to as ‘settlement coins’ under the proposed regulation, is, from a legal perspective, indistinguishable from traditional cash deposits. Third, payments may be settled in e-money tokens, as defined in the proposal for a regulation of the European Parliament and of the Council on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 (hereinafter referred to as the ‘proposed Markets in Crypto-assets regulation’).

3.3.2. Settlement of payments in central bank money

The ECB considers that settlement in central bank money should be the default requirement for DLT market infrastructures, and therefore an exemption from this requirement should be possible only in cases where the relevant DLT market infrastructure operator proves that this settlement method is not available and practicable.

3.3.3. The Eurosystem offers settlement of securities transactions on a delivery versus payment basis in central bank money to T2S participants. While the ECB remains open to innovation and to further explore the potential of innovative technologies in the context of the provision of securities settlement services, the potential settlement in central bank money of DLT transferable securities transactions in T2S would be subject to limitations arising from the current technological constraints as well as contractual and regulatory framework governing the provision of T2S services (\(^{14}\)). In this vein, it is worth highlighting that the specific design features and exemptions characterising each DLT SSS operated by a CSD will be taken into account when assessing the fulfilment of the T2S eligibility criteria (\(^{15}\)) if a CSD wishes to join T2S.


\(^{10}\) See paragraph 3.18.5 of CPMI-IOSCO Principles for financial market infrastructures, Principle 18 on Access and participation requirements details the operational, financial, legal and risk-management requirements for participation that should be taken into account by an FMI, mentioning also the possibility that an FMI admits non-regulated entities. In such a case, the FMI should (i) take into account any additional risks that may arise from such participation and (ii) design its participation requirements and risk-management controls accordingly.

\(^{11}\) See Article 25 of MiFID II on the assessment of the suitability and appropriateness of financial instruments for investors.


3.3.4. Where settlement of DLT transferable securities transactions is intended to take place outside T2S, DLT SSSs may also be subject to some of the limitations in ensuring settlement in central bank money arising from the current technological constraints as well as contractual and regulatory framework, depending on the specific design features of the DLT SSS and the applicable ECB Guidelines (\(^4\)). The same considerations concerning settlement outside T2S apply mutatis mutandis to operators of DLT MTFs.

3.3.5. **Settlement of payments with persons that are not licensed as credit institutions**

Under the CSD Regulation, where it is not practical and available to settle through central bank accounts, a CSD may offer to settle the cash payments for all or part of its SSS through accounts opened with a credit institution or through the CSD’s own accounts. If a CSD offers to settle in accounts opened with a credit institution or through its own accounts, it must do so in accordance with the provisions of Title IV of the CSD Regulation (\(^7\)). While the proposed regulation provides that a CSD operating a DLT SSS must identify, measure, monitor, manage, and minimise any counterparty risk arising from the use of commercial bank money or e-money tokens (\(^8\)), the requirements for ensuring a sound cash settlement through commercial bank money (or e-money tokens) in the proposed regulation are very general, when compared to the requirements under the CSD Regulation (\(^9\)). The same also applies, mutatis mutandis, to operators of DLT MTFs. Significantly, the proposed regulation (\(^8\)) provides that the competent authority may exempt a CSD operating a DLT SSS from the provisions on cash settlement under the CSD Regulation (\(^9\)), provided that the CSD ensures delivery versus payment. This would appear to implicitly open the door to exempting a CSD settling the cash leg of securities transactions through its own accounts from the requirement to be licensed as a credit institution under Directive 2013/36/EU of the European Parliament and of the Council (hereinafter referred to as the ‘Capital Requirements Directive’) (\(^9\)) and from the provisions governing banking-type ancillary services under the CSD Regulation (\(^9\)). Along the same lines, the broad formulation of this provision under the proposed regulation (\(^9\)) could also be interpreted as implicitly opening the door to exempting a CSD from settling the cash leg of securities transactions through accounts opened with a licensed credit institution.

3.3.6. Under the Capital Requirements Directive, persons or undertakings that are not credit institutions are prohibited from carrying out the business of taking deposits or other repayable funds from the public. This prohibition does not apply to ‘cases expressly covered by national or Union law’ (\(^9\)). It is suggested that the possibility for an exemption under the proposed regulation from the application of Article 40 and Title IV of the CSD Regulation on cash settlement is insufficiently clear to qualify as a ‘case expressly covered by Union law’ that would allow a person that is not a credit institution to receive deposits from the public. In view of this apparent conflict between the proposed regulation and the Capital Requirements Directive, the Union legislative bodies need to expressly clarify the exact scope of the derogation from the cash settlement provisions of the CSD Regulation that a CSD operating a DLT SSSs (or an operator of a DLT MTF (\(^7\))) may apply for.

3.3.7. In the absence of specific details on how settlement of payments in e-money tokens may take place, participants in a CSD operating a DLT SSS would be able to open accounts directly with the CSD for the purposes of settling the cash leg of a securities transaction in e-money tokens, or alternatively the CSD operating a DLT SSS and its participants would open an account with a third party providing services relating to e-money tokens. In these two cases, the CSD or the third party would be the issuer of e-money tokens and would ensure that settlement of the cash leg takes place in e-money tokens. In this respect, it is worth noting that, under the proposed Markets in Crypto-assets regulation, e-money tokens can only be issued either by credit institutions or e-money institutions (\(^9\)). In the absence of any provision to the contrary under the proposed regulation, the ECB

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(\(^4\)) Guideline (EU) 2015/310 (ECB/2014/60) and Guideline ECB/2012/27.
(\(^5\)) See Article 40(2) and Article 54 of the CSD Regulation.
(\(^6\)) See Article 40(3) of the proposed regulation.
(\(^7\)) See recital (24) and Article 5(5) of the proposed regulation. See also for DLT MTFs recital (16) and Article 4(3)(f) of the proposed regulation.
(\(^8\)) See Article 40 of the CSD Regulation.
(\(^10\)) See Title IV of the CSD Regulation and Section C of the Annex thereto.
(\(^11\)) See Article 5(5) of the proposed regulation.
(\(^12\)) See Article 9 of the Capital Requirements Directive.
(\(^13\)) See Article 4(3) of the proposed regulation.
(\(^14\)) See Article 43 of the proposed Markets in Crypto-assets regulation.
understands that the exemption provided under the proposed regulation with respect to the cash settlement provisions of the CSD Regulation \(^{(4)}\) is not intended to exempt a CSD or a third party issuing e-money tokens and settling the cash leg of securities transactions through its own accounts from the licensing requirements under the proposed Markets in Crypto-assets regulation. The same considerations on the settlement of payment obligations in e-money tokens apply mutatis mutandis to the operators of DLT MTFs \(^{(2)}\). It is difficult to understand why the Union legislative bodies would want to require, on the one hand, that e-money tokens can only be issued either by credit institutions or e-money institutions, and, on the other hand, to implicitly open the door to settling the cash leg of securities transactions in traditional cash or settlement coins through accounts opened with persons which are not licensed as credit institutions.

3.3.8. In deciding whether it wishes to open the door to settling the cash leg of securities transactions through accounts opened with persons which are not licensed as credit institutions, the Union legislative bodies may wish to have regard to the CPMI-IOSCO Principles for Financial Market Infrastructures (PFMIs) \(^{(2)}\). In particular, under CPMI-IOSCO Principle 9 of the PFMIs (Money settlements), if money settlement does not occur in central bank money, CPMI-IOSCO Principle 9 only envisages settlement in commercial bank money or on the FMI's own books. Specifically, CPMI-IOSCO Principle 9 provides that if the FMI conducts money settlements on its own books, it should minimise and strictly control its credit and liquidity risks. In such an arrangement, an FMI offers cash accounts to its participants, and a payment or settlement obligation is discharged by providing an FMI's participants with a direct claim against the FMI itself. The credit and liquidity risks associated with a claim against an FMI are therefore directly related to the FMI's overall credit and liquidity risks. One way an FMI could minimise these risks is to limit its activities and operations to clearing and settlement and closely related processes. Further, to settle payment obligations, the FMI could be established as a special-purpose financial institution and limit the provision of cash accounts to participants only. Depending on local laws, these special-purpose financial institutions would generally be required to have banking licences and be subject to prudential supervision \(^{(4)}\).

3.3.9. Under the proposed regulation, natural persons may directly participate in DLT market infrastructures. If the cash leg of a securities transaction were to occur on the books of a person who is not a licensed credit institution, this would have the consequence that the cash accounts held by natural persons, as well by legal persons such as micro, small and medium-sized enterprises, with DLT market infrastructures would not benefit from the deposit guarantee scheme protection under Directive 2014/49/EU of the European Parliament and of the Council (hereinafter referred to as the 'Deposit Guarantee Schemes Directive') \(^{(4)}\) and of the depositor preference under Directive 2014/59/EU of the European Parliament and of the Council \(^{(4)}\) (hereinafter referred to as the 'BRRD'). The Deposit Guarantee Schemes Directive and the depositor preference under the BRRD only apply to deposits in the form of a credit balance which results from funds left in an account or from temporary situations deriving from normal banking transactions and which a credit institution is required to repay \(^{(4)}\). Taking account of CPMI-IOSCO Principle 9, in particular the minimisation and strict control of credit and liquidity risks arising from money settlements using FMI's, such a situation would not seem to provide a sufficient means for safeguarding the funds of natural persons placed with operators of DLT market infrastructures. In addition, the proposed regulation does not establish any threshold to limit the ability of operators of DLT market infrastructures to hold funds of natural persons and micro, small and medium-sized enterprises, despite the possibility that such persons may wrongly believe that their funds represent deposits enjoying the benefit of the Deposit Guarantee Schemes Directive and the depositor preference under the BRRD.

3.3.10. Finally, the Union legislative bodies may wish to consider whether risks to the stability of the financial system might emerge should exemptions from the licensing requirements provided for under the Capital Requirements Directive, the CSD Regulation and the proposed Markets in Crypto-assets regulation in connection with (a) carrying out the business of taking deposits or other repayable funds from the public, (b) the provision of banking-type ancillary services and (c) the issuance of e-money tokens, be granted under the proposed regulation.

\(^{(4)}\) See Article 5(5) of the proposed regulation and Article 40 of the CSD Regulation.

\(^{(2)}\) See Article 4(3) of the proposed regulation.


\(^{(2)}\) See paragraph 3.9.7 of the CPMI-IOSCO Principles for Financial Market Infrastructures (PFMIs).


\(^{(4)}\) See Article 2(1), point (3), of the Deposit Guarantee Schemes Directive in conjunction with Article 2(1), points (4) and (5), and Articles 5 and 6 of the same Directive and Article 2(1), points (94) and (95), and Article 108 of the BRRD.
The exemptions from the licensing requirements mentioned would result in a shift from credit institutions to non-bank actors of activities typically confined within the remit of the banking sector. Consequently, participants in DLT market infrastructures, and potentially participants in existing SSSs or MTFs managed by the same operators of DLT market infrastructures, including connected FMIs, would, as a result, be exposed to higher credit and liquidity risks because the strict regulatory and prudential requirements provided for credit institutions do not apply to non-bank operators. Ultimately, DLT market infrastructures would benefit from a lower level and range of safeguards that may not just hamper their overall soundness but more broadly the deployment of DLT technology in the post-trading sector.

3.3.11. Risk management requirements applicable to banking-type ancillary services

The CSD Regulation imposes very restrictive requirements on banking-type ancillary services, as the provision of such services involves significant financial risks, including intra-day credit and liquidity risks. The role CSDs play in the financial markets and their related systemic importance justify stringent risk management requirements aimed at ensuring resilience in extreme but plausible circumstances. In particular, as previously noted, only CSDs authorised as credit institutions and designated credit institutions (\(^9\)) observing the requirements of Title IV of the CSD Regulation (\(^9\)) are allowed to provide banking-type ancillary services. The ECB notes that the proposed regulation allows for the possibility that a CSD that is licensed as a credit institution and operates a DLT SSS, or which relies on a credit institution for the provision of banking-type ancillary services, is exempted from the requirements of Article 40 of the CSD Regulation, including those defined in Title IV of the same Regulation. The scope of the exemption is not defined in the proposed regulation, so it is understood that a DLT SSS operated by a CSD may be exempted from some or all of the requirements of Title IV of the CSD Regulation, including those in relation to the scope of banking-type ancillary services, the management of credit and liquidity risks and capital surcharges (\(^9\)).

Depending on the scope of an exemption, the level of risk which DLT SSSs may be exposed to would vary and, in particular, if the exemption covers all Title IV requirements, the risks could be very significant. However, the requirements (\(^9\)) applicable for conducting settlement in commercial bank money, as set out in the proposed regulation, are only general and may not ensure application of risk management measures commensurate to the risks incurred. In view of the foregoing, the ECB proposes that the Union legislative bodies should specify in more detail the scope of the exemptions to Article 40 of the CSD Regulation and the conditions to be met for receiving such exemptions. The same should also apply, mutatis mutandis, to operators of DLT MTFs, where they do not conduct settlement in central bank money, having regard to the considerations on ensuring a level playing field between DLT MTFs and DLT SSSs, as noted in paragraph 1.3.

3.4. Insolvency protections under the Settlement Finality Directive

Under the proposed regulation, the operation by a CSD of a DLT SSS may not be tantamount to the operation of a ‘system’, as defined under the Settlement Finality Directive, not least because, according to the proposed regulation, natural persons are eligible participants in a DLT SSS (\(^9\)). In such a case, the operation of a DLT SSS would not be regarded as an extension of activities or services under the CSD Regulation (\(^9\)), but as an additional activity or service that should be subject to the assessment and authorisation process under the CSD Regulation. The ECB has three remarks to make in this respect. First, the ECB recalls the pivotal role of the concept of (legal) finality for the protection of settlement systems participants from the disruptive consequences of insolvency proceedings against other participants, and for the reduction of systemic risks emanating from the operation of FMIs. If a DLT SSS were not to qualify as a ‘system’, within the meaning of the Settlement Finality Directive, the insolvency protections thereunder would not apply to the DLT SSS itself. Second, the ECB notes that the proposed regulation is not clear as to what legal measures it may need to take when the same CSD is simultaneously operating an SSS and a DLT SSS (e.g. to ring-fence the two by entrusting their operation to separate legal entities). Should finality risks materialise for unprotected DLT SSSs and/or their participants, these could spill over to other regular SSSs operated by the same CSD, as well as to its participants. Such risks could materialise, for instance, where one or more entities participate in both a regular and a DLT SSS operated by the same CSD. In view of the foregoing, it

\(^{9}\) Under the CSD Regulation, a credit institution that offers to settle the cash payments for part of the CSD’s SSS is exempted from some requirements of Title IV only where the total value of such cash settlement through accounts opened with that credit institution does not exceed certain thresholds over a period of time. See Article 54(4) and (5) of the CSD Regulation.

\(^{9}\) In particular, Article 54(4)(d) of CSD Regulation provides that the credit institution used as a cash settlement agent can be used only to provide banking-type ancillary services as defined in the CSD Regulation and not to carry out any other activities.

\(^{9}\) The exemption from the requirement to have a banking licence is discussed in paragraphs 3.3.5 to 3.3.10.

\(^{9}\) See the final subparagraph of Article 5(5) of the proposed regulation.

\(^{9}\) See Article 2(a) and (d) of the Settlement Finality Directive and recital (23) and Article 5(8) of the proposed regulation.

\(^{9}\) See Article 19 of the CSD Regulation and recital (33) of the proposed regulation.
would be helpful for the proposed regulation to require a CSD operating a DLT SSS (whether or not in parallel to the operation of a regular SSS) to clearly explain the insolvency and settlement finality risks to which its participants are exposed, as well as any mitigating measures that the CSD has put in place in order to mitigate such risks. Third, the ECB sees merit in the proposed regulation explicitly catering for the involvement of the relevant authorities in the assessment of the risks to which the parallel operation of regular and DLT SSSs may give rise, as part of the CSD authorisation process.

3.5. **Level playing field between operators of DLT market infrastructures**

The proposed regulation refers briefly to the issue of preventing and addressing settlement fails, which is pivotal for promoting settlement discipline and the safe and efficient settlement of transactions (9). There is a significant asymmetry between the requirements applicable to a DLT MTF and the provisions set out in the CSD Regulation (10). The absence of uniform requirements on settlement fails may trigger a race to the bottom among operators of DLT MTFs and may ultimately result in a more favourable treatment of DLT MTF operators compared to CSDs and a lower level of settlement safety for DLT MTF participants compared to CSD participants.

3.6. **Exit strategy for operators of DLT market infrastructures and removal of DLT transferable securities from trading**

The proposed regulation refers in broad terms to a transition strategy i.e. an exit strategy that operators of DLT market infrastructures must have in place in the event that the permission or some of the exemptions granted have to be withdrawn or otherwise discontinued, or in the event of any voluntary or involuntary cessation of the business (11). Where permissions or exemptions are revoked or the market valuation of DLT transferable securities exceeds certain thresholds, an operator of a DLT market infrastructure may have to undertake substantial changes, the implementation of which would likely require a significant period of time. Moreover, if there is no alternative operator of a DLT market infrastructure able or willing to ensure continuity of services, the withdrawal of a specific permission or of any of the exemptions granted (12) may not be implemented in practice, contrary to the spirit of the proposed regulation. In view of the foregoing, the ECB proposes that the Union legislative bodies should provide greater detail on the specific content of the exit strategy and the timeline for its implementation. In addition, the proposed regulation should be supplemented with specific procedures that would be applicable in the case of removal of DLT transferable securities from trading on a DLT MTF, as well as in the case of a breach of the EUR 200 million market capitalisation limit for the admission to trading on a DLT MTF. Most importantly, it should be clearly indicated how investors holding the relevant DLT transferable securities would be protected in such cases. It should be indicated whether the issuer (or its largest shareholder) should conduct a buy back of the relevant DLT transferable securities, whether such an operation would be mandatory also for investors, and how the fair price would be determined in such cases. Alternatively, the ECB suggests that there should be specific arrangements in place for the conversion of such DLT transferable securities into ‘non-DLT’ transferable securities registered in a CSD.

3.7. **Interplay with the proposed Markets in Crypto-assets regulation**

3.7.1. There is a potential mismatch between the proposed regulation and the scope of application of the proposed Markets in Crypto-assets regulation. In the settlement models for e-money tokens described in paragraph 3.3.7, e-money token issuers and/or service providers, which, under the proposed Markets in Crypto-assets regulation, fall under the umbrella definitions of crypto-assets issuers and crypto-assets services providers, would de facto provide services in relation to financial instruments, namely DLT transferable securities. If this is the case, it seems that such services are neither regulated under the proposed regulation nor under the proposed Markets in Crypto-assets regulation.

3.7.2. Furthermore, under the proposed Markets in Crypto-assets regulation, e-money tokens classified as significant are subject to additional requirements (13). In particular, with regard to the custody of reserve assets (14), issuers of significant e-money tokens must ensure at all times that the reserve assets are not encumbered or pledged as a ‘financial collateral arrangement’, a ‘title transfer financial collateral arrangement’ or a ‘security financial collateral arrangement’.

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(9) See Article 4(3)(g) of the proposed regulation.
(10) See Article 6(3) and (4) and Article 7 of the CSD Regulation.
(11) See Articles 6(6) and 3(5) of the proposed regulation.
(12) See Articles 7(6) and 8(6) of the proposed regulation.
(13) See Articles 33 and 52 of the proposed Markets in Crypto-assets regulation.
(14) See Article 33(1)(b) and Article 52(a) of the proposed Markets in Crypto-assets regulation.
4. **Prudential supervisory aspects**

4.1. The ECB and the relevant NCA are the competent authorities exercising specified prudential supervisory powers under Regulation (EU) No 575/2013 of the European Parliament and of the Council (\(^4\)) (hereinafter referred to as the ‘Capital Requirements Regulation’) and the Capital Requirements Directive. In addition, the SSM Regulation confers specific tasks on the ECB concerning the prudential supervision of credit institutions within the euro area and makes the ECB responsible for the effective and consistent functioning of the Single Supervisory Mechanism (SSM) within which specific supervisory responsibilities are distributed between the ECB and the participating NCAs (\(^5\)). In particular, the ECB has the task of authorising and withdrawing the authorisation of all credit institutions. For significant credit institutions, the ECB also has the task, among others, to ensure compliance with the relevant Union laws imposing prudential requirements on credit institutions, including the requirement to have in place robust governance arrangements, such as sound risk management processes and internal control mechanisms (\(^6\)). To this end, the ECB is given all supervisory powers to intervene in the activity of credit institutions that are necessary for the exercise of its functions.

4.2. The proposed regulation sets out the basic requirements for the operation of DLT market infrastructures, together with a series of exemptions that can be requested from specific requirements embedded in MiFID II, Regulation (EU) No 2014/600 and the CSD Regulation. This means that investment firms also licensed as credit institutions and market operators may request permission from the national competent authority to operate DLT market infrastructures for the purposes, inter alia, of registering and settling DLT transferable securities. Furthermore, the proposed regulation requires the operators of DLT market infrastructures to cooperate with the competent authorities entrusted with the granting of specific permissions as well as with the European Securities and Markets Authority (ESMA) (\(^7\)).

4.3. The ECB notes that the current approach taken with regard to the authorisation process fosters equal treatment for credit institutions and non-credit institution operators alike and represents a step forward towards risk-based supervision taking account of the activities performed by a given entity. Having said that, while the proposed regulation does not envisage the involvement of the ECB (as prudential supervisor) in the authorisation and exemption process, it may be relevant for the ECB, from a prudential supervision perspective, to receive information from the national competent authority with regard to significant credit institutions that wish to operate a DLT market infrastructure. Therefore, it is suggested that the proposed regulation should include an obligation on the national competent authority to notify the prudential supervisor, including the ECB for significant credit institutions, of whether or not permissions and exceptions are granted, as well as where corrective measures are imposed. For the same reasons, it is suggested that the proposed regulation should include the applicable prudential supervisor among the recipients of the regular reporting by the operators of a DLT market infrastructure (\(^8\)).

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\(^7\) See Article 4(1)(e) and Article 6(4) of Regulation (EU) No 1024/2013.

\(^8\) See Article 9 of the proposed regulation.

\(^9\) See Article 9(4) of the proposed regulation.
Where the ECB recommends that the proposed regulation is amended, specific drafting proposals are set out in a separate technical working document accompanied by an explanatory text.

This opinion will be published on EUR-Lex.

Done at Frankfurt am Main, 28 April 2021.

The President of the ECB
Christine LAGARDE