2nd April 2020

DG FISMA,
Rue de Spa 2,
1000,
Bruxelles,
Belgium

Re: The public consultation on an EU regulatory framework for crypto-assets

Channel: Online Submission
Contact: fisma-crypto-assets@ec.europa.eu

About GDF

GDF a leading industry body that promotes the adoption of best practices for crypto and digital assets and digital finance technologies through the development of conduct standards, in a shared engagement forum with market participants, policymakers and regulators. Established in 2018, GDF has convened a broad range of industry participants, with 300+ global community members - including some of the most influential digital asset and token companies, academics and professional services firms supporting the industry.

Consultation response contributors

Name	Title & Organisation
Jeff Bandman	Board Member and Global Regulatory Affairs Lead at GDF
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Background for this public consultation

As stated by President von der Leyen in her political guidelines for the new Commission, it is crucial that Europe grasps all the potential of the digital age and strengthens its industry and innovation capacity, within safe and ethical boundaries. Digitalisation and new technologies are significantly transforming the European financial system and the way it provides financial services to Europe's businesses and citizens. Almost two years after the Commission adopted the Fintech action plan in March 2018, the actions set out in it have largely been implemented.

In order to promote digital finance in Europe while adequately regulating its risks, in light of the mission letter of Executive Vice-President Dombrovskis, the Commission services are working towards a new Digital Finance Strategy for the EU. Key areas of reflection include deepening the Single Market for digital financial services, promoting a data-driven financial sector in the EU while addressing its risks and ensuring a true level playing field, making the EU financial services regulatory framework more innovation-friendly, and enhancing the digital operational resilience of the financial system.

This public consultation, and the parallel public consultation on digital operational resilience, are first steps to prepare potential initiatives which the Commission is considering in that context. The Commission may consult further on other issues in this area in the coming months.

GDF Response

The GDF consultation response contributors provided answers to the questions in the survey most relevant to our sphere of experience.

Question 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)?

Answer:
Yes

Please explain your reasoning (if needed):
GDF agrees that the scope should not be expanded to digital assets so as to include the digital representation of other assets. Doing so would create a boundary-less scope for regulatory activity. GDF considers that digital assets such as electronic supermarket vouchers, airline points or an electronic copy of a film, whether transferable or not, is not intended to be caught under the remit of this initiative.

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

Answer:
Yes

If yes, please indicate the best way to achieve this classification (non-legislative guidance, regulatory classification, a combination of both…). Please explain your reasoning:
GDF notes that it is imperative to have common classifications of crypto-assets for its seamless use across borders, this is something that GDF has been advocating through the development of its codes of conduct. Whilst the market has been converging on common terminology in recent months, there is still a need for greater certainty. GDF considers that non-legislative guidance is the most helpful format for this in order to accommodate market need and support the dynamic and flexible nature of crypto-assets. However, there are crypto-assets such as basket-backed stablecoins that are completely new and outside the current regulatory regime that would require greater intervention to develop the relevant rules.

Question 7: What would be the features of such a classification?

When providing your answer, please indicate the classification of crypto-assets and the definitions of each type of crypto-assets in use in your jurisdiction (if applicable).

Answer:
GDF has used slightly different terminology for the classification of tokens – payment

tokens, financial asset tokens and consumer tokens. GDF has characterised them as follows:

Payment Tokens

These are crypto-assets that have intrinsic features designed to serve as a general purpose store of value or medium of exchange. By "general purpose," we mean that these tokens are intended to serve as a medium of exchange for generally any goods, services, or assets, and thus are similar to more traditional currencies in that respect. Such general-purpose Payment Tokens could be created and distributed by any number of organisations or methods, including:

1. Central banks or other government departments
2. Commercial banks
3. Companies issuing something akin to card-based payment instruments (e.g. Apple Pay)
4. New models and distributions - e.g. a decentralised network creates, distributes and operates a crypto payment token, as was the case with Bitcoin.

These tokens may be the native token of a particular blockchain protocol, in which case they may be issued as part of the set-up of that protocol or as rewards to "miners" who help operate the protocol.

Financial Asset Tokens

These crypto-asset have intrinsic features that are designed to represent assets typically of an underlying financial type, such as participations in companies or earnings streams, or an entitlement to dividends or interest payments. In terms of their economic function, these tokens are analogous to equities, bonds or derivatives (listed market instruments). In addition, so-called alternative assets (e.g. Real Estate, Private Equity, Art etc.) are increasingly being discussed as good candidates for being Financial Asset Tokens due to the increased process efficiency that could be brought to private placements and the ability to access global liquidity pools.

Although variations may exist, a typical Asset Token would be issued by a business or entity in order to raise capital. Examples of Financial Asset Tokens include but are not limited to tokens that represent:

- Common stock in a company
- A right to receive a certain percentage of operating revenues
- A corporate bond
- Fractional or full ownership of real estate or private equity assets

Consumer Tokens

Consumer Tokens are crypto-assets with intrinsic features that are inherently consumptive in nature, meaning they are designed to be used or consumed in some way, such as providing access to a limited set of goods, services, or content. In essence, consumer tokens can serve as or power next-generation consumer goods, services, and platforms.

Like other tokens, consumer tokens have extrinsic features. The most well-known example of a Consumer Token is probably Ether, which was marketed, sold, and serves as "fuel" for the Ethereum blockchain. Ether is needed to pay for transactions and computation and is also provided to miners as a reward for securing and validating transactions. Thus, under our taxonomy, Ether has characteristics of a coupon, license, and reward. Whilst "Ether" clearly demonstrates consumptive behaviour or activities, it can also be used as a payment instrument or be used to model financial agreements. This complexity is viewed differently by global authorities. To manage this geographical diversity of approach and to bring increased industry clarity Global Digital Finance has produced the "crypto-asset Code of Conduct". In practice, once a platform is available, Consumer Tokens represent a wide spectrum of use cases, ranging from enabling the creation and consumption of content on a specific platform, or as a means of blockchain to blockchain communication.

Most current consumer tokens involve one or more of the following types of intrinsic features:

- Consumer Ownership Rights: Tokens can themselves be a natively digital consumer good, such as a tokenised collectible like a badge for online gameplay or a unique digital collectible that does not exist in the physical world, such as a virtual pet; or they can represent ownership of an analog (i.e. not digital or on the blockchain) good, such as a traditional baseball card. In both cases, the token can confer ownership in the corresponding good and/or represent the good.
- Consumer Coupon Rights: Tokens that provide a partial or complete discount on particular goods, services, or content, in the physical world or in the virtual world, e.g. file storage on a given tokenpowered network or electricity provided to retail customers.
- Consumer Activity Rights: Tokens that involve rights or obligations related to an individual user's activities on a token-powered network. With regard to consumer activity rights, we contemplate at least two current subcategories:
    - Reward: Tokens that serve as a form of reward or payment for performed activities. In the cases of online platforms, the tokens earned can also be used to access features or get benefits on the platform. In the case of physical systems, the tokens may act like "frequent flyer miles" to be redeemed for services or goods.

- License: Tokens that serve as a means to access or perform certain activities related to an online service. Analogies in the analog world may include a software license, taxi medallions for New York City taxis, or occupational licensing and certifications for certain vocations. In the virtual world, this could include a token which allows access to a content-driven website. License rights may also include relationships similar to those we are all familiar with, such as a membership to a wholesale club, or the right to participate in a book club of the month.

The term “utility token” has also been used to describe what this document calls “consumer tokens.” The GDF community selected the term “consumer” instead of “utility,” because it properly emphasises that for a Consumer Token to become successful, it needs adoption by actual consumers who will use and consume the token. We recognise that this implies the need for potential consumer protections. Whilst many of these tokens are still early as are the platforms that support them, the Global Digital Finance community aims to strike the right balance of enabling innovation whilst being committed to efficient, fair and transparent market activity (where reasonably applicable).

Question 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’?

Answer:

No

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

As highlighted above, GDF refers to these tokens as payment tokens, financial asset tokens and consumer tokens. However, GDF also notes the advice from ESMA in January 2019 referring to payment-type, investment-type and utility-type tokens. Whilst developing the GDF taxonomy, one of the key findings was that categorising crypto-asset often led to them not falling neatly within one category and therefore being excluded from the regulatory perimeter. There could be a similar issue when trying to create an EU classification for this. Therefore, GDF determines that the Commission proposal should provide regulatory guidance that clarifies the regulatory perimeter so as to ascertain token treatment.

With regards to hybrid tokens, GDF understands this to cover both tokens which may change their characteristics throughout the token lifecycle such as Ethereum as explained in the example above and tokens that have characteristics of more than one token type. For example, if a token was purchased with the purpose of permitting access to a future service it would be classified as a utility token but it may also have been bought for investment purposes and therefore be classified as being a hybrid. It is unclear to us how to differentiate this from a digital pass to an event, for example. We would consider that a token which is being bought in advance of a service being actually available and which is transferable should be deemed a speculative investment, and therefore considered for regulation in the security or investment token category. However, a service access/use type token which is bought for use once a service is actually available is not a speculative investment, whether or not it is actually used for the purpose intended or ultimately transferred to another person in a secondary sale for subsequent use. GDF seeks clarification as to whether hybrid tokens will have to comply with the more stringent legal requirements, or if they will have to meet the legal obligation of the feature it covers predominantly.

Question 10: In your opinion, what is the importance of each of the potential benefits related to crypto-assets listed below?

Please rate each proposal from 1 to 5, 1 standing for "not important at all" and 5 for "very important".

	1	2	3	4	5	No opinion
Issuance of utility tokens as a cheaper, more efficient capital raising tool than IPOs			x			
Issuance of utility tokens as an alternative funding source for start-ups			x			
Cheap, fast and swift payment instrument					x	
Enhanced financial inclusion					x	
Crypto-assets as a new investment opportunity for investors		x				

Improved transparency and traceability of transactions					x	
Enhanced innovation and competition				x		
Improved liquidity and tradability of tokenised 'assets'					x	
Enhanced operational resilience (including cyber resilience)				x		
Security and management of personal data				x		
Possibility of using tokenisation to coordinate social innovation or decentralised governance			x			
Other						

Please justify your reasoning (if needed):

With regards to the first utility token question – GDF notes that Investment Tokens that don't otherwise have features of equity, debt or derivatives might not be regulated to the same degree as issuance of those securities (or their equivalent crypto-assets), or even if they are so regulated, they might still be issued more efficiently and in a more disintermediated manner on DLT, thereby being quicker and cheaper for startups and tech projects. However, from a regulatory perspective in an "IPO" scenario they are being issued as investment instruments and need to be considered for regulation as such.

With regards to the second utility token question – GDF notes that non-transferable utility tokens which are issued in advance of the launch of a project by a tech start-up may be a helpful way of raising funds.

For the four categories that GDF has allocated as very important (5):

1. Use of crypto-assets, in particular fiat or cash equivalent securities backed stablecoins, as a swift, efficient, traceable and transparently auditable payment method, is very important in our view, especially when considered alongside standardisation (i.e. the adoption of standardised payment transaction and messaging rails) as to: use cases between financial institutions, the "value side" of unlocking the benefits of smart contracts for online transactions, potential digital stores of value and an accessible bridge for the broader population from fiat into a fully digitised economy.

2. Financial inclusion goes to the heart of this technology, the ability to reach locations and individuals the traditional finance sector cannot reach is a strong benefit of this technology.
3. Improved transparency and traceability is a very important feature of crypto-assets because it will make business more efficient, removing the burden of certain transaction review loops like audit and some compliance processes. Combined with effective cyber-security, it will also assist with denomination of responsibility, the combat of money-laundering and other financial crime.
4. The ability of crypto-assets to aid fractionalisation and to create liquidity in otherwise illiquid assets is also key to the development of the asset class and extraction of the whole value of what these instruments can potentially offer. This is both potentially beneficial in terms of greater financial inclusion and to enhance the range of liquid asset options available for purposes of smoothing trading operations and avoiding liquidity squeezes.

Question 11: In your opinion, what are the most important risks related to crypto-assets?

Please rate each proposal from 1 to 5, 1 standing for "not important at all" and 5 for "very important".

	1	2	3	4	5	No opinion
Fraudulent activities					x	
Market integrity (e.g. price, volume manipulation...)				x		
Investor/consumer protection			x			
Anti-money laundering and CFT issues				x		
Data protection issues				x		
Competition issues		x				
Cyber security and operational risks					x	
Taxation issues		x				
Energy consumption entailed in crypto-asset activities				x		

Financial stability			x			
Monetary sovereignty/monetary policy transmission			x			
Other						

Please justify your reasoning (if needed):

GDF notes that "Stablecoins" are a relatively new form of payment tokens whose price is meant to remain stable through time. Those "stablecoins" are typically asset-backed by real assets or funds (such as short-term government bonds, fiat currency, commodities, real estate, securities…) or by other crypto-assets. They can also take the form of algorithmic "stablecoins" (with algorithm being used as a way to stabilise volatility in the value of the coin). While some of these "stablecoins" can qualify as 'financial instruments' under MiFID II or as e-money under EMD2, others may fall outside the scope of EU regulation. A recent G7 report on 'investigating the impact of global stablecoins' analysed "stablecoins" backed by a reserve of real assets or funds, some of which being sponsored by large technology or financial firms with a large customer base. The report underlines that "stablecoins" that have the potential to reach a global scale (the so-called "global stablecoins") are likely to raise additional challenges in terms of financial stability, monetary policy transmission and monetary sovereignty, among others. Users of "stablecoins" could in principle be exposed, among others, to liquidity risk (it may take time to cash in such a "stablecoin"), counterparty credit risk (issuer may default) and market risk (if assets held by issuer to back the "stablecoin" lose value).

Question 12: In your view, what are the benefits of "stablecoins" and "global stablecoins"?

Please explain your reasoning (if needed):

GDF regards fiat or cash equivalent securities backed stablecoin, as a swift, efficient, traceable and transparently auditable payment method, as very important, especially when considered alongside standardisation (i.e. the adoption of standardised payment transaction and messaging rails) as to: use cases between financial institutions, providing the "value side" of unlocking the benefits of smart contracts for DLT-based online transactions, potential digital stores of value and an accessible bridge for the broader population from fiat into a fully digitized economy. All stablecoins also offer the opportunity of unlocking payment transactability without traditional institutional-based accounts, therefore having the potential of bringing financial services to the mobile phone-owning unbanked.

GDF notes that global stablecoins may have particular enhancements in terms of their actual "stability" (with a basket backed product, there is greater ability to trade levels of collateral assets up and down to smooth out short term fluctuations), they may also offer a more internationally neutral, broadly attractive digital currency option by moving away from the more geo-political fiat product. In terms of international exchange, one of the criticisms of single fiat stablecoin is that there is little point in the context of international exchange, if the stablecoin version of the currency has to be exchanged with other currencies anyway. However, a broader basket backed stablecoin may be able to overcome this by offering a single shared reference point for common value. For users in countries with local currencies that have high volatility and/or that are subject to exchange control making their own international transactability more limited, a global stablecoin which may hold value more effectively and be widely accepted as payment could be very beneficial in circumventing local economic challenges.

Question 13: In your opinion, what are the most important risks related to "stablecoins"?

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
Fraudulent activities					x	
Market integrity (e.g. price, volume manipulation...)			x			
Investor/consumer protection			x			
Anti-money laundering and CFT issues			x			
Data protection issues					x	
Competition issues		x				
Cyber security and operational risks					x	
Taxation issues		x				
Energy consumption			x			

Financial stability				x		
Monetary sovereignty/monetary policy transmission					x	
Other						

Please explain in your answer potential differences in terms of risks between "stablecoins" and "global stablecoins" (if needed):

- GDF notes that CBDCs would be issued on a national government footing, most stablecoin projects that have been considered to date are intended to be launched by private institutions, formed in one way or another to be more or less centralised, more or less robustly governed. Some of the major issues facing these projects are issues of cyber-security and fraud – without trust and confidence in the stablecoin product, they are unlikely to be adopted on a broad enough basis to make them viable in the long term. The same also goes for institutional payments type stablecoins here. Without very robust cyber-security and the ability to prevent fraud and theft, these solutions will not be workable.
- GDF considers that broader public payments solutions, data protection and data privacy are also very high on the agenda of issues facing the space. If the fully auditable, all-seeing, data driven platforms on which stablecoin products are built are owned by private companies, then there may well be data privacy risks for users. Whereas weak cyber-security and fear of fraud may cause users to avoid the product altogether, issues with data privacy do not necessarily motivate avoidance and therefore present a high risk in terms of potential exploitation.
- With regards to global stablecoins, GDF notes that monetary sovereignty and some of the levers available for macro-economic control with respect to monetary policy, could be reduced by a very broadly adopted basket-backed coin, both for currencies not involved at all in the collateral and those whose currencies become only the partial basis for the transactions which are undertaken with the product.
- GDF regards the risks on financial stability for global stablecoins to be rated as a 4, however, this will be rated as a 1 for stablecoins in general – owning to the size and reach of the network.
- Finally GDF considers that in the short term, resolving the position of international authorities on the taxation of digital assets is a high priority and some adjustments are likely to be required. However, in the longer term, GDF anticipates that transparent and readily auditable value transactions over DLT-based platforms are likely to offer improvements in tax assessment and collections.

Question 19: Do you consider that the issuer or sponsor of crypto-assets marketed to EU investors/consumers should be established or have a physical presence in the EU?

Answer:
No

Please explain your reasoning (if needed):
When referring to crypto-assets as being marketed, we assume that this is to be understood similar to securities. GDF are not of the view that establishment or physical presence necessarily should be required by an issuer or a sponsor of a crypto-asset. The nature of crypto-assets is global, and a requirement of establishment or physical presence would reduce the inherent value of the crypto-assets functionality. Having that said, GDF recognises that depending on the underlying structure of the crypto-asset, certain regulatory requirement should be in place, but we believe that this can be achieved by other way than requiring establishment or physical presence (for instance a cross-border approval procedure similar to approval procedures applicable to third-party countries).

Question 21: Should an issuer or a sponsor of crypto-assets be required to provide information (e.g. through a 'white paper') when issuing crypto-assets?

Answer:
Yes

Please indicate the entity that, in your view, should be responsible for this disclosure (e.g. the issuer/sponsor, the entity placing the crypto-assets in the market) and the content of such information (e.g. information on the crypto-asset issuer, the project, the rights attached to the crypto-assets, on the secondary trading, the underlying technology, potential conflicts of interest...).
GDF suggests that the issuance of crypto-assets should be accompanied by a disclosure document which could be in the form of a white paper including general requirements. This is something that GDF included in our Principles of Token Sales code of conduct as well as the code of conduct for Security Token Offerings.

Question 22: If a requirement to provide the information on the offers of crypto-assets is imposed on their issuer/sponsor, would

you see a need to clarify the interaction with existing pieces of legislation that lay down information requirements (to the extent that those rules apply to the offers of certain crypto-assets, such as utility and/or payment tokens)?

Please rate each proposal from 1 to 5, 1 standing for "completely irrelevant" and 5 for "highly relevant".

	1	2	3	4	5	No opinion
The Consumer Rights Directive[28]		x				
The E-Commerce Directive[29]			x			
The EU Distance Marketing of Consumer Financial Services Directive[30]		x				
Other (please specify) Prospectus requirements/Investor protection rules					x	

Please explain your reasoning and indicate the type of clarification (legislative/non legislative) that would be required.

GDF determines that unless information disclosure requirements can follow from existing requirements, it would be advisable to put in place specific information disclosure requirements for crypto-assets in order to avoid any misconceptions.

GDF considers that the disclosure requirements should be similar to those pertaining to securities.

Question 23: Beyond any potential obligation as regards the mandatory incorporation and the disclosure of information on the offer, should the crypto-asset issuer or sponsor be subject to other requirements?

Please rate each proposal from 1 to 5, 1 standing for “completely irrelevant” and 5 for "highly relevant ".

	1	2	3	4	5	No opinion

The managers of the issuer or sponsor should be subject to fitness and probity standards					x	
The issuer or sponsor should be subject to advertising rules to avoid misleading marketing/promotions					x	
Where necessary, the issuer or sponsor should put in place a mechanism to safeguard the funds collected such as an escrow account or trust account					x	See comment below
Other						

Please explain your reasoning (if needed):
GDF considers that the potential requirement of the issuer or sponsor having in place a mechanism to safeguard the funds collected should be essential. In light of "*stable*coin", GDF considers this safeguard mechanism as appropriate.

Question 24: In your opinion, what would be the objective criteria allowing for a distinction between "stablecoins" and "global stablecoins" (e.g. number and value of "stablecoins" in circulation, size of the reserve…)?

Please explain your reasoning (if needed):
As per the G7 report the term global stablecoins refers to those that are developed by existing firms who already have a large customer base and therefore have the ability to scale rapidly. GDF considers that whilst the network is important it is more the underlying use and the size of the footprint that is significant. Therefore, the distinguishing factor must be around the distribution and the reserves. It will be important to establish an objective criteria for the thresholds as to what constitutes a 'substantial footprint' as referenced in the G7 paper and apply measures accordingly.

Question 25: To tackle the specific risks created by "stablecoins" and "global stablecoins", what are the requirements that could be imposed on their issuers and/or the manager of the reserve?

Please indicate for both "stablecoins" and "global stablecoins" if each proposal is relevant (leave it blank if you have no opinion).

	"Stablecoins"		"Global stablecoins"	
	Relevant	**Not relevant**	**Relevant**	**Not relevant**
The reserve of assets should only be invested in safe and liquid assets (such as fiat-currency, short term-government bonds…)	Agree		Agree	
The issuer should contain the creation of "stablecoins" so that it is always lower or equal to the value of the funds of the reserve		Not relevant (disclosure requirement relevant)		Not relevant (disclosure requirement relevant)
The assets or funds of the reserve should be segregated from the issuer's balance sheet	Agree		Agree	
The assets of the reserve should not be encumbered (i.e. not pledged as collateral)	Agree, subject to certain carve-outs		Agree, subject to certain carve-outs	
The issuer of the reserve should be subject to prudential requirements rules (including capital requirements)	Depends on the extend other safeguard measures are in place		Depends on the extend other safeguard measures are in place	
The issuer and the reserve should be subject to specific requirements in case of insolvency or when it decides to stop operating	Agree		Agree	

Obligation for the assets or funds to be held in custody with credit institutions in the EU		No reason to be EU institutions		No reason to be EU institutions
Periodic independent auditing of the assets or funds held in the reserve	Agree		Agree	
The issuer should disclose information to the users on (i) how it intends to provide stability to the "stablecoins", (ii) on the claim (or the absence of claim) that users may have on the reserve, (iii) on the underlying assets or funds placed in the reserve	Agree		Agree	
The value of the funds or assets held in the reserve and the number of stablecoins should be disclosed periodically	Agree		Agree	
Requirements to ensure Interoperability across different distributed ledgers or enable access to the technical standards used by the issuer	No opinion		No opinion	
Other				

Please illustrate your response (if needed):

GDF notes that "Stablecoins" could be used by anyone (retail or general purpose) or only by a set of actors, i.e. financial institutions or selected clients of financial institutions (wholesale). The scope of uptake may give rise to different risks. The G7 report on "investigating the impact of global stablecoins' stresses that *"Retail stablecoins, given their public nature, likely use for high-volume, small-value payments and potentially high adoption rate, may give rise to different risks than wholesale stablecoins available to a restricted group of users"*.

Question 26: Do you consider that wholesale “stablecoins” (those limited to financial institutions or selected clients of financial institutions, as opposed to retail investors or consumers) should receive a different regulatory treatment than retail “stablecoins”?

Answer:
No

Please explain your reasoning (if needed):
GDF considers that, unless particular reasons support the specific need for a wholesale stablecoin (could be particular functionalities for inter-bank transactions), we do not see a reason to create a subset of stablecoins in the form of wholesale stablecoins. From a general point of view, we believe the level playing field being created for stablecoins should apply to all users, regardless of the nature of the user.

Question 29: In your opinion, what are the main risks in relation to crypto-to-crypto and fiat-to-crypto exchanges?

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			x			
Lack of adequate governance arrangements, including operational resilience and ICT security					x	
Conflicts of interest arising from other activities	x					
Absence/inadequate record keeping of transactions		x				
Absence/inadequate complaints or redress procedures are in place		x				
Bankruptcy of the exchange					x	

Inadequate own funds to repay the consumers					x	
Losses of users' crypto-assets through theft or hacking					x	
Users suffer loss when the exchange they interact with does not exchange crypto-assets against fiat currency (conversion risk)					x	
Absence of transparent information on the crypto-assets proposed for exchange			x			
Other						

Please explain your reasoning (if needed):

GDF considers that the main risks which would apply to securities exchange will be equally applicable to crypto exchanges with added risk of losses due to token theft by hackers, however, this can be managed with appropriate regulatory and capital requirements.

Question 30: What are the requirements that could be imposed on exchanges in order to mitigate those risks?

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						
Exchanges should be subject to governance arrangements (e.g. in terms of operational resilience and ICT security)			x			
Exchanges should segregate the assets of users from those held on own account			x			
Exchanges should be subject to rules on conflicts of interest	x					

Exchanges should be required to keep appropriate records of users' transactions				x		
Exchanges should have an adequate complaints handling and redress procedures			x			
Exchanges should be subject to prudential requirements (including capital requirements)					x	
Exchanges should be subject to advertising rules to avoid misleading marketing/promotions				x		
Exchanges should be subject to reporting requirements (beyond AML/CFT requirements)				x		
Exchanges should be responsible for screening crypto-assets against the risk of fraud		x				
Other						

Please indicate if those requirements should be different depending on the type of crypto-assets available on the exchange and explain your reasoning (if needed):
As highlighted in a previous response, GDF are of the view that requirements for securities exchanges will be similar to the requirements needed for crypto exchanges. In particular:

1. Regulatory capital requirements – exchanges must meet adequate capital requirement to cover market changes as well as security breaches
2. AML/KYC requirements – crypto exchanges should (and in most cases currently are) required to comply with AML/KYC regulations

Question 31: In your opinion, what are the main risks in relation to the custodial wallet service provision?

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
No physical presence in the EU				x		
Lack of adequate governance arrangements, including operational resilience and ICT security					x	
Absence or inadequate segregation of assets held on the behalf of clients					x	
Conflicts of interest arising from other activities (trading, exchange)			x			
Absence/inadequate record keeping of holdings and transactions made on behalf of users				x		
Absence/inadequate complaints or redress procedures are in place					x	
Bankruptcy of the custodial wallet provider					x	
Inadequate own funds to repay the consumers				x		
Losses of users' crypto-assets/private keys (e.g. through wallet theft or hacking)					x	
The custodial wallet is compromised or fails to provide expected functionality				x		
The custodial wallet provider behaves negligently or fraudulently					x	
No contractual binding terms and provisions with the user who holds the wallet				x		
Other						

Please explain your reasoning (if needed):

GDF considers that the fact that a custodial wallet service provider would not be physically present in a specific EU Jurisdiction should not be a risk, however, it could cover specific risks which should be addressed by the proposal.

GDF are currently in the process of finalising its Principles for Custody 'Custodial Wallets' which is in public consultation. Mirroring this, the proposal should require adequate governance arrangements, including operational resilience and other policies, procedures and processes (as well as related documentation) related to IT security and safety proceedings enhancing protection against cyber-attacks (and against other IT risks). Additionally, crypto-asset should be subject to specific good conduct, transparency, conflict of interest, know-your-customer as well as other rules protecting its clients against any risk of misconduct and fraud. Specific segregation rules and record-keeping / traceability rules should also be implemented taking into account the very specificities of this service to enhance customer's protection.

Question 32: What are the requirements that could be imposed on custodial wallet providers in order to mitigate those risks?

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
Custodial wallet providers should have a physical presence in the EU			x			
Custodial wallet providers should be subject to governance arrangements (e.g. in terms of operational resilience and ICT security)					x	
Custodial wallet providers should segregate the asset of users from those held on own account					x	
Custodial wallet providers should be subject to rules on conflicts of interest					x	
Custodial wallet providers should be required to keep appropriate records of users' holdings and transactions				x		
Custodial wallet providers should have an adequate complaints handling and redress procedures					x	

Custodial wallet providers should be subject to capital requirements					x	
Custodial wallet providers should be subject to advertising rules to avoid misleading marketing/promotions					x	
Custodial wallet providers should be subject to certain minimum conditions for their contractual relationship with the consumers/investors				x		
Other						

Please indicate if those requirements should be different depending on the type of crypto-assets kept in custody by the custodial wallet provider and explain your reasoning (if needed):

Requiring physical presence of wallet providers would entail substantial costs for small companies which may not be able to afford such costs. GDF considers that for custodial wallet providers to be supervised by the relevant supervisory authorities they need not have a physical presence in the EU. For example, the proposal may wish to consider protecting EU-based consumers.

As custodial wallet providers would be in possession of client's assets (or have any form of control over these assets), they should implement all security requirements to ensure that these assets are returned to the clients on demand. This includes operational resilience and ICT security and segregation of assets. The requirements could be modelled on those applicable to custodians.

In addition, crypto-asset holders should benefit from the same protection as investors, *i.e.* the custodial wallet providers should act in their best interest; not be subject to conflict of interests; be equipped to adequately handle complaints raised by holders; and should be subject to marketing/promotions rules. In order for the crypto-asset holders to know their rights, they should enter into transparent, clear and exhaustive terms and conditions.

Further, GDF considers that the crypto asset custody service should be monitored by the relevant authorities, which would ensure for instance that they keep record of the transactions made on behalf of their clients. They should also be subject to capital requirements in order to ensure that they are able to absorb losses.

GDF however does not believe that the custodial wallet provider should be subject to different requirements depending on the crypto-asset kept in custody, as all clients should be protected the same way regardless of the asset involved.

Question 34: In your view, what are the services related to crypto-assets that should be subject to requirements?

Please rate each proposal by level of relevance from 1 to 5, 1 standing for "completely irrelevant" and 5 for "highly relevant".
When referring to execution of orders on behalf of clients, portfolio management, investment advice, underwriting on a firm commitment basis, placing on a firm commitment basis, placing without firm commitment basis, we consider services that are similar to those regulated by Annex I A of MiFID II.

	1	2	3	4	5	No opinion
Reception and transmission of orders in relation to crypto-assets		X				
Execution of orders on crypto-assets on behalf of clients		X				
Crypto-assets portfolio management		X				
Advice on the acquisition of crypto-assets		X				
Underwriting of crypto-assets on a firm commitment basis		X				
Placing crypto-assets on a firm commitment basis		X				
Placing crypto-assets without a firm commitment basis		X				
Information services (an information provider can make available information on exchange rates, news feeds and other data related to crypto-assets)					X	
Processing services, also known as 'mining' or 'validating' services in a DLT environment (e.g. 'miners' or validating 'nodes' constantly				X		

work on verifying and confirming transactions)						
Distribution of crypto-assets (some crypto-assets arrangements rely on designated dealers or authorised resellers)		X				
Services provided by developers that are responsible for maintaining/updating the underlying protocol				X		
Agent of an issuer (acting as liaison between the issuer and to ensure that the regulatory requirements are complied with)		X				
Other services						

Please illustrate your response by underlining the potential risks raised by these services if they were left unregulated and by identifying potential requirements for those service providers.

GDF considers that where crypto-asset services, akin to investment services and activities in Annex I Section A of MiFID II, are being undertaken, there are grounds based on the risks and responsibilities associated with these services to bring these actors within the regulatory perimeter.

Where crypto-assets are properly classified as financial instruments for the purposes of Annex I Section C of MiFID II, these investment services and activities would necessitate the service provider to obtain authorisation from a relevant competent authority. Bringing into the regulatory perimeter crypto-assets order execution, advice and transmission activities would ensure consistent consumer protection and market standards across the wide categorisation of crypto-assets. This would remove the incentive to re-classify security tokens away from the financial services regulatory perimeter as equivalent safeguards would be in place for other categories of crypto-asset. Other services, such as information services have lower risks and consistent with exemptions in MiFID II for media organisations, should be exempt from registration and/or authorisation.

GDF notes that the Commission's proposal may wish to analyse the effectiveness of an optional regime as per the approach taken by France with the PACTE Law. Under the PACTE Law, digital asset service providers (DASPs) providing the service of digital asset custody or purchase / sale of digital assets in exchange for legal tender are subject to mandatory registration with the AMF. Conversely, DASPs only providing other services on digital assets (e.g. operation of a digital assets trading platform, purchase/sale of

digital assets against other digital assets, reception and transmission of orders or placement on digital assets) may apply for an optional license, subject to compliance with a set of rules (internal control procedures, resilient IT system, transparent pricing policy, etc.).

Question 36: Should the activity of making payment transactions with crypto-assets (those which do not qualify as e-money) be subject to the same or equivalent rules as those currently contained in PSD2?

Answer:
Yes

Explain your reasoning if needed:
GDF notes that PSD 2 provides for various disclosures as well as rights for payment service users when entering into a payment transaction. "Payment transaction" is defined broadly in PSD 2 as meaning means an act, initiated by the payer or on his behalf or by the payee, of placing, transferring or withdrawing funds, irrespective of any underlying obligations between the payer and the payee. "Funds" means banknotes and coins, scriptural money or electronic money. The definition of "funds" does not extend to crypto-assets where the crypto-assets cannot be defined as the aforementioned.

The disclosure requirements in framework contracts and the rights of payment service users should also be available to payees and payers who engage in payment transactions using crypto-assets. By way of example, Article 73 of PSD 2 provides for the Payment Service Provider's liability for unauthorised payment transactions. Concepts such as the payer's capped liability for unauthorised payment transactions resulting from the loss of payment instrument may be analogous to the use of cryptographic private keys.

GDF notes that pure speculative investment transactions would not be included as payment transactions and would therefore be out of scope. GDF considers that at this stage, given the relatively limited adoption of crypto-assets for use in payment transactions, extending PSD 2's scope to "funds" would result in limited additional payment service user protection at this time. It would, however, be forward-thinking and give users added confidence in choosing alternatives when engaging in payment transactions. Corporates, as with existing payment transactions, should be able to continue to opt-out of certain protections and information requirements of PSD 2. It would also require Payment Service Provides (like merchant acquirers) to consider alternatives to card-based transactions more actively in terms of updating their business models beyond card schemes.

Question 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 'crypto-assets' that could be used in a potential bespoke regulation on crypto-assets)?

Answer:
No

Please explain your reasoning if needed:
No, whilst GDF are firm advocates of aligning definitions, including all digital (or virtual) representations of assets within scope would create a potential boundary-less scope for regulatory activity. The regulatory considerations around crypto-assets (consistent with the definition of "virtual currency" in MLD5) arise due to the particular features of multi-party transferability and cryptographic security of data transmission. Other arguably "digital assets", such as electronic supermarket vouchers, airline points or an electronic copy of a film may or may not be transferable, in various circumstances, but do not warrant regulatory consideration within this initiative.

Question 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.
Disintermediation has resulted in certain gaps in regulatory coverage and associated consumer safeguards. P2P transactions is one area where this gap is obvious. P2P crypto-asset platforms will not be classified as crypto-asset exchanges but should be in-scope of the EU AML/CFT framework given the particular risks of spoofing, dirty money and lack of verification associated with P2P transactions. Equally, crypto-to-crypto exchanges should also be caught within scope of the EU AML/CFT framework. GDF urges the Commission to also consider crypto custodians, kiosks and ATMs, which GDF considers should also fall within the remit of the framework.

Question 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?

Answer:
Yes

Please explain your reasoning (if needed):
GDF welcomes the extension of MLD5 into making crypto-asset exchanges and custodian wallet providers “obliged entities” however notes that gaps remain in the ecosystem. Frequently, it is other entities in the ecosystem that may represent a higher risk of money laundering or counter-terrorist financing. These should also be included in scope.

Question 44: In your view, how should the AML/CFT risks arising from peer-to-peer transactions (i.e. transactions without intermediation of a service provider) be mitigated?

GDF considers that to the extent there is some intermediary, that intermediary should be brought within scope of the EU AML/CTF framework. For example, a website that provide the functionality of users to upload/download. Whilst the website may describe itself as only a platform, they should be brought within scope of KYC/CDD/EDD requirements.

Where the P2P transactions does not involve intermediation, analogy can be drawn from securities law where hawking is banned and promotional activity is otherwise controlled and regulated. Where appropriateness checks have been undertaken, pure P2P transactions should not be included within the scope of any proposed extension of the regulatory framework, to the extent that regulation would apply to the individuals.

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

Answer:
Yes

Please explain your reasoning (if needed):
GDF notes the pseudo-anonymous nature of certain crypto-assets is seen as one of the key benefits for potential money laundering, counter-terrorist financing, tax evasion or other criminal acts. Should the FATF requirements be introduced, a consequence may

be a diminished role for so-called “privacy” coins.

Question 46: In your view, do you consider it relevant that the following requirements are imposed as conditions for the registration and licensing of providers of services related to crypto-assets included in section III. B?

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
Directors and senior management of such providers should be subject to fit and proper test from a money laundering point of view, meaning that they should not have any convictions or suspicions on money laundering and related offences				X		
Service providers must be able to demonstrate their ability to have all the controls in place in order to be able to comply with their obligations under the anti-money laundering framework				X		

Question 54: Please highlight any recent market developments (such as issuance of security tokens, development or registration of trading venues for security tokens...) as regards security tokens (at EU or national level)?

GDF notes the following non-exhaustive list of developments:

- Security tokens being issued on private placement basis
- Limited issuances of utility tokens (within limited network only)
- Stablecoin projects are in development, but few have launched
- Increased demand for digital assets exchanges (focused on institutional investors) looking to become regulated in order to enter security tokens market

Question 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			x			
Provide a definition of a security token at EU level				x		
Provide guidance at EU level on the main criteria that should be taken into consideration while qualifying a crypto-asset as security token					x	
Other						

Question 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)					x	
Other						

Please explain your reasoning (if needed):
GDF refers back to the answer given to question 8 in section I of this response:

As highlighted above GDF refers to these tokens as payment tokens, financial asset tokens and consumer tokens, however GDF also notes the advice from ESMA in January 2019 referring to payment-type, investment-type and utility-type tokens. Whilst developing the GDF taxonomy, one of the key findings was that categorising crypto-asset often led to them not falling neatly within one category and therefore being excluded from the regulatory perimeter. There could be a similar issue when trying to create an EU classification for this. Therefore, GDF determines that the Commission proposal should provide regulatory guidance that clarifies the regulatory perimeter so as to ascertain token treatment.

With regards to hybrid tokens, GDF understands this to cover both tokens which may change their characteristics throughout the token lifecycle (such as Ethereum as explained in the example above) and tokens that have characteristics of more than one token type. For example, if a token was purchased with the purpose of permitting access to a future service it would be classified as a utility token but it may also have been bought for investment purposes and therefore be classified as being a hybrid. It is unclear to us how to differentiate this from a digital pass to an event, for example. We would consider that a token which is being bought in advance of a service being actually available and which is transferable should be deemed a speculative investment, and therefore considered for regulation in the security or investment token category. However, a service access/use type token which is bought for use once a service is actually available is not a speculative investment, whether or not it is actually used for the purpose intended or ultimately transferred to another person in a secondary sale for subsequent use. GDF seeks clarification as to whether hybrid tokens will have to comply with the more stringent legal requirements or whether they will have to meet the legal obligation of the feature it covers predominantly.

Question 64: Do you think that the current scope of investment services and activities under MiFID II is appropriate for security tokens?

Completely appropriate	
Rather appropriate	X

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

Please explain your reasoning (if needed):
GDF considers that the scope of investment services and activities in Section A of Annex I of MiFID II is adequate to encompass the array of services associated with security tokens.

Question 65: Do you consider that the transposition of MiFID II into national laws or existing market practice in your jurisdiction would facilitate or otherwise prevent the use of DLT for investment services and activities?

It will not prevent the use of DLT.

Please explain your reasoning (if needed):
GDF notes the development of DLT in the UK has progressed despite the implementation of MiFID II. The regulatory framework is flexible enough to encompass an array of business models that incorporate DLT. The Financial Conduct Authority's regulatory sandbox and Project Innovate have been instrumental in providing a framework for the testing of DLT based products with live customers.

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):

Trading venue definitions – GDF highlights the potential issues:

1. In general, the notions of an MTF and an OTF are suitable for DLT-based security tokens.

2. Even though in principle DLT-based trading platforms could qualify for regulated market status, in practice, there are few market infrastructures operating under this status per EEA Member State. The lack of a regulated

market supporting DLT-based securities may create barriers to entry for crypto-asset market operators, especially if they seek to become publicly listed.

3. The treatment of DLT-based trading platforms with hybrid business models is not always straight-forward. Some hybrid platforms provide for the matching of orders but not their execution itself, which may be processed through smart contracts. It is unclear whether these platforms would qualify as RMs, MTFs, OTFs or not.

4. In addition, with regards to platforms with decentralised business models, the lack of a clearly identified operator and the reliance on self-executing pieces of code raise specific issues, e.g. which market participant should be an authorised investment firm?

GDF highlights the potential issues relating to the operation of crypto-asset trading venues:

1. Custody services – Many of the operational models of crypto-asset trading platforms involve custody of (i.e., holding, controlling and safekeeping) participant assets, which may include crypto-assets and/or fiat currency or funds. However, asset custody functions are not usually performed by trading venues but rather by intermediaries, custodians, transfer agents and clearing houses. The performance of these functions directly by crypto-asset trading platforms may mean that these platforms should be subject to additional requirements to mitigate potential risks. These risks could include:

    - Operational failure – the system may be compromised such that participant assets are lost or inaccessible (e.g., due to a cyber-attack).
    - Theft, loss or inaccessibility of private keys - private keys are compromised (e.g., due to a cyber-attack or breach, or by an action of a crypto-asset trading venues insider) or lost resulting in stolen or inaccessible assets.
    - Co-mingling of assets – the assets of the crypto-asset trading venue may be co-mingled with those of participants and/or participant assets may be pooled, meaning that in the event of a default, investor assets may not be fully protected.
    - Inaccurate record-keeping - the crypto-asset trading venue may not accurately reconcile records or properly account for assets.
    - Insufficient assets to meet liabilities – the crypto-asset trading venue may not maintain sufficient assets to cover participants' claims (i.e., the crypto-asset trading venue is not able to meet withdrawal demands).

2. Conflicts of interest – GDF highlights that certain crypto-asset trading venues position themselves to provide end-to-end services including, for example, the admittance and trading of the crypto-asset, settlement, custody, market-making and advisory services. Therefore, they may have additional conflicts of interest, which should be managed appropriately.

3. Settlement of trades – GDF noted that there are challenges resulting from the Central Securities Depository Regulation (CSDR). The CSDR requires issuers to register transferable securities with an authorised central securities depository (CSD) when these are traded on EU trading venues. This is problematic as at the moment there is no market infrastructure to support this (authorised DLT-based CSD or authorised CSD that supports DLT-based securities).

Question 66: Do you think that current scope of investor protection rules (such as information documents and the suitability assessment) are appropriate for security tokens?

Answer:
Yes

Question 68: Would you see any merit in establishing specific requirements on the marketing of security tokens via social media or online?

Please explain your reasoning (if needed):
GDF considers that the MiFID II framework is already sophisticated enough to take into account a variety of ways that security tokens can be marketed. “Marketing communications” in Article 24 of MiFID II is not defined. Further specific obligations in respect to marketing communications as applied in the Delegated Regulation (Organisational Requirements) should be able to be applied to the offerings of security tokens.

GDF warns that being more prescriptive on forms of media may result in the legislative framework being “stuck in time” and not as sufficiently adaptive to new media.

Question 69: Would you see any particular issue (legal, operational) in applying MiFID investor protection requirements to security tokens?

Answer:
No

Question 88: Would you see any particular issue (legal, operational, technical) with applying the following definitions 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
Definition of 'central securities depository' and whether platforms can be authorised as a CSD operating a securities settlement system which is designated under the SFD					x	
Definition of 'securities settlement system' and whether a DLT platform can be qualified as securities settlement system under the SFD					x	
Whether records on a DLT platform can be qualified as securities accounts and what can be qualified as credits and debits to such an account					x	
Definition of 'book-entry form' and 'dematerialised form					x	
Definition of settlement (meaning the completion of a securities transaction where it is concluded with the aim of discharging the obligations of the parties to that transaction through the transfer of cash or securities, or both)					x	

What could constitute delivery versus payment in a DLT network, considering that the cash leg is not processed in the network					x	
What entity could qualify as a settlement internaliser					x	

Please explain your reasoning (if needed):
GDF notes that in the current legal framework, CSDs can only service security tokens insofar and to the extent they qualify as securities within the meaning of CSDR (i.e. financial instruments within the meaning of MiFID II), because: (a) the services listed in the Annex to CSDR only relate to securities; and (b) the non-banking type ancillary services which are not explicitly mentioned in Section B of the Annex to CSDR for which the CSD can be licensed, still need to contribute to enhancing the safety, efficiency and transparency of the securities markets. If the security tokens qualify as securities within the meaning of CSDR, a CSD can accept them for deposit. In such case, the CSD can only render the services permitted under CSDR.

GDF notes that from a legal certainty perspective, CSDs would benefit from a clear regulatory or statutory position as to which tokens classify as financial instruments within the meaning of MiFID II, and therefore as securities within the meaning of CSDR.

This question, along with the other questions raised in the table above cannot be answered with absolute certainty today. However, we believe that other jurisdictions, such as France, Luxembourg and the US State of Wyoming have demonstrated that legal certainty and clarity can be achieved with minimal statutory intervention.

Question 89: Do you consider that the book-entry requirements under CSDR are compatible with security tokens?

Answer:
Yes
Please explain your reasoning (if needed):
GDF understands the question as whether the creation of a security on a DLT ledger can be considered a “book-entry on a register/account” or a security “in dematerialised form” under article 1 (1) (4) and article 3 (1) and (2) of CSDR.

GDF sees no reason why not. Other jurisdictions, such as France, Luxembourg and the US State of Wyoming have demonstrated that with minimal statutory intervention, clarity can be achieved in this respect

Question 90: 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 settlement periods for the settlement of certain types of financial instruments in a securities settlement system	x					
Rules on measures to prevent settlement fails	x					
Organisational requirements for CSDs	x					
Rules on outsourcing of services or activities to a third party			x			
Rules on communication procedures with market participants and other market infrastructures			x			
Rules on the protection of securities of participants and those of their clients	x					
Rules regarding the integrity of the issue and appropriate reconciliation measures	x					
Rules on cash settlement						x
Rules on requirements for participation						x
Rules on requirements for CSD links						x
Rules on access between CSDs and access between a CSD and another market infrastructure			x			
Other (including other provisions of CSDR, national rules applying the EU acquis,						x

supervisory practices, interpretation, applications…)						

Please explain your reasoning (if needed):
GDF notes the following questions which would benefit from statutory or regulatory clarification:

(i) article 30 of CSDR (outsourcing): in which circumstances do entities involved in the validation process give rise to an "outsourcing" for the purposes of article 30 of the CSDR?

(ii) article 35 of CSDR (communication with participants and other market infrastructures): what is meant by "internationally accepted standards for communication procedures"?

GDF notes that it is unclear as of yet whether the mere usage of a DLT-based SSS by a CSD is considered outsourcing under CSDR. It can be argued that this is not the case based on article 19 of CSDR, the CSDR requirements relating to outsourcing only apply where a third party delivers services to the CSD which would normally be undertaken by the CSD itself in the course of its usual business. Therefore, if a third party merely licenses "off the shelf" (standard) software packages to the CSD and provides standard support for such packages, the CSD did not outsource any of its services to such third party. However, regulators may consider the use by a CSD of settlement software from a blockchain start-up (Software as a Service) as a form of outsourcing insofar as the data relating to the transactions realised through such software is not hosted on the CSD's own servers but for example in the cloud. On the other hand, cloud service providers currently argue that they only deliver a standard service (different from the services which their clients normally render in the course of their usual business) which should be considered as the provision of a utility service instead of outsourcing.

Question 92: Would you see any particular issue (legal, operational, technical) with applying the following definitions in the SFD or its transpositions into national law 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
Definition of a securities settlement system			x			
Definition of system operator			x			

Definition of participant	x					
Definition of institution	x					
Definition of transfer order	x					
What could constitute a settlement account	x					
What could constitute collateral security	x					
Other						x

Please explain your reasoning (if needed):
GDF notes that it is important to keep the distinction between legal finality and probabilistic finality in mind.

The SFD is designed to ensure legal settlement finality. This is the legally defined moment at which the transfer of an asset or financial instrument, or the discharge of an obligation, is irrevocable and unconditional and not susceptible to being unwound following the bankruptcy or insolvency of a participant. In traditional systems, settlement finality is a clear and well-defined point in time, backed by a strong legal basis. For DLT arrangements, settlement finality may not be as clear. In arrangements that rely on a consensus algorithm to effect settlement finality, there may not necessarily be a single point of settlement finality. Further, the applicable legal framework may not expressly support finality in such cases.

GDF notes that in a DLT environment, the term 'finality' often refers to 'operational' or 'probabilistic' finality. Broadly, it signifies that once a transaction is included in the blockchain, there is certainty that it will not be undone later by the emergence of an alternative "longer" blockchain which does not include the subject transaction. In some DLT arrangements, it can take some time to update and synchronise state changes to a ledger. The first instance of an update, for example, may not represent operational settlement because it may take time for consensus to be achieved across the nodes in the synchronisation of ledgers. In arrangements that use a proof-of-work model, settlement is probabilistic. That is, the more times the transaction is confirmed in the ledger, the less likely it will be revoked. Operational settlement becomes more complex if it involves the delivery of one asset against another, for example, the exchange of securities against the corresponding cash amounts or exchange of one currency for another. In many arrangements involving an exchange of value, another financial market infrastructure is typically involved.

GDF notes that the platform upon which security tokens are settled must qualify as a "system" in the meaning of article 2 (a) of the SFD (an '***SSS***'). Therefore, the following

conditions should be complied with: (i) the platform is underpinned by a formal arrangement between three or more participants (or "nodes") of the DLT ledger (without counting the central entity operating the (permissioned) DLT system) with common rules and standardised arrangements for the execution of transfer orders between the participants; (ii) it is governed by the law of an EU member state chosen by the participants, it being understood that the participants may only choose the law of an EU member state in which at least one of them has its head office; (iii) the national legislator formally designates the platform as an SSS. To achieve this, the platform has to be operated by a duly licensed CSD complying with the CSDR requirements; and (iv) the platform is not operated by a central counterparty (CCP) whose activity consists of the execution of transfer orders.

Question 94: SFD sets out rules on conflicts of laws. According to you, would there be a need for clarification when applying these rules in a DLT network?

Please explain your reasoning:

Yes, GDF considers that applying the law dependent on where the property is situated does not translate well when applied to security tokens. The location of an asset constituted on a DLT ledger – which by definition is distributed and can span several jurisdictions – is not clear. Locating the register of security tokens on a blockchain is not meaningful, as a DLT ledger is stored and reproduced at every node in the blockchain. The PREMA/PROPA approach could potentially be applied, provided that it can be made clear who the Relevant Administrator/Operating Authority is. A CSD could offer such clarity by positioning itself clearly as the Relevant Administrator/Operating Authority. GDF suggest that one way to demonstrate this is for the CSD to be responsible (and liable) for acting as "master node" on the blockchain i.e., the CSD will be the "validating node" on the network. In such a case, it is more likely (albeit, this would have to be analysed further) that the law of the jurisdiction where the CSD is established, would apply to the proprietary aspects of any transactions in security tokens on that Blockchain.

Question 105: Do the provisions of the EU AIFMD legal framework in the following areas are appropriately suited for the effective functioning of DLT solutions and the use of security tokens?

Please rate each proposal from 1 to 5, 1 standing for "not suited" and 5 for "very suited".

	1	2	3	4	5	No opinion

AIFMD provisions pertaining to the requirement to appoint a depositary, safe-keeping and the requirements of the depositary, as applied to security tokens;		X				
AIFMD provisions requiring AIFMs to maintain and operate effective organisational and administrative arrangements, including with respect to identifying, managing and monitoring the conflicts of interest;		X				
Employing liquidity management systems to monitor the liquidity risk of the AIF, conducting stress tests, under normal and exceptional liquidity conditions, and ensuring that the liquidity profile and the redemption policy are consistent;		X				
AIFMD requirements that appropriate and consistent procedures are established for a proper and independent valuation of the assets;		X				
Transparency and reporting provisions of the AIFMD legal framework requiring to report certain information on the principal markets and instruments.					X	
Other						

Please explain your reasoning:

AIF Depositaries – In general, the requirement to appoint a AIF depositary which is separate from the AIFM is suited to security tokens. However, GDF notes the following issues:

1. Types of entities acting as depositories – Currently, AIFMD requires that an AIF depositary must be one of the following:
    - an EU credit institution (for example, an EU bank);
    - an investment firm authorised under the MiFID II Directive (2014/65/EU) and subject to the same capital requirements as credit institutions. This includes investment banks, but excludes most investment managers and agency brokers; or
    - a prudentially regulated and supervised institution of a type that is eligible to be a UCITS depositary under the UCITS Directive (2009/65/EC) (Article 21(3)).

GDF highlights that the effect of this is that the principal providers of depositary services for most types of EU AIFs are EU banks or EU investment banks. This creates barriers to entry to DLT-based solutions as they have to rely on the collaboration of incumbent institutions, who may not be able to support the technology for the safekeeping of DLT-based security tokens. In addition, currently, there is no global standard for the prudential treatment of exposures to crypto-asset for banks or other regulated entities. This may be an additional reason that prudential regulated entities, such as banks and investment firms, may be reluctant to act as depositaries of AIFs.

2. Location of depositaries – The AIFMD imposes limits on who may be a depositary based on where it is established.
    - The depositary of an EU AIF must either have its registered office or a branch in the AIF's home member state (being the member state where the AIF was first authorised or registered or, if it is not authorised or registered, where it has its registered office or head office) (Article 21(5)(a)).
    - The depositary of a non-EU AIF must either have its registered office or a branch in the AIFM's home member state (or, once the third country provisions are effective, member state of reference, in the case of a non-EU AIFM) (Article 21(5)(b)). Alternatively, the depositary may be established in the non-EU country in which the AIF is established if certain conditions are met.

GDF notes that in a DLT context, it is problematic to link the location of the depositary with the 'location' of the AIFs, due to the distributed nature of security tokens.

Valuation of assets – GDF considers that the regulatory framework relating to valuation of assets may create challenges in a crypto-asset context:

1. The traditional valuation methods developed for shares or derivatives are not always suitable for the valuation of crypto-assets.

2. The crypto-asset investment community has so far struggled to define a cohesive framework for valuing these assets.

GDF highlights that as a result of the diversity of tokens, the methods are adjusted to the specific nature of the relevant token to get a realistic result. This might create a challenge for supervisors (and thus for asset managers seeking supervisory approval) as one classic supervisory concern is that models or methods are specifically developed with the aim of downplaying risk. As in traditional finance, absolute and relative valuation methods have been developed for crypto-asset.

Question 106: Do you consider that the effective functioning of DLT solutions and/or use of security tokens is limited or constrained by any of the AIFMD provisions?

Answer:
Yes

If yes, please provide specific examples with relevant provisions in the EU acquis. Please explain your reasoning (if needed):
Yes, GDF considers that AIFMD marketing provisions (Articles 31-42 AIFMD), the applicable rules regarding the marketing of AIFs within the EU, depend on the location of the AIF (the rules differ depending whether this is an EU or non-EU AIF). However, it is problematic to link marketing rules with the 'location' of security tokens/AIFs, due to the distributed nature of certain DLT-based tokens.

10. The Undertakings for Collective Investment in Transferable Securities Directive (UCITS Directive)

GDF notes that the UCITS Directive 77 applies to UCITS established within the territories of the Member States and lays down the rules, scope and conditions for the operation of UCITS and the authorisation of UCITS management companies. The UCITS directive might be perceived as potentially creating challenges when the assets are in the form of 'security tokens', relying on DLT.

For example, GDF notes that under the UCITS Directive, an investment company and a management company (for each of the common funds that it manages) shall ensure that a single depositary is appointed. The assets of the UCITS shall be entrusted to the depositary for safekeeping. For crypto-assets that are not 'security tokens' (those which do not qualify as financial instruments), the rules for 'other assets' apply under the UCITS Directive. In such a case, the depositary needs to ensure the safekeeping (which involves verification of ownership and up-to-date recordkeeping) but not the custody. This function could arguably cause perceived uncertainty where such assets are security tokens.

Directive 77 - Undertaking for Collective Investment in Transferable Securities Directive (2009/65/EC)

Question 107: Do the provisions of the EU UCITS Directive legal framework in the following areas are appropriately suited for the effective functioning of DLT solutions and the use of security tokens?

Please rate each proposal from 1 to 5, 1 standing for "not suited" and 5 for "very suited".

	1	2	3	4	5	No opinion
Provisions of the UCITS Directive pertaining to the eligibility of assets, including cases where such provisions are applied in conjunction with the notion “financial instrument” and/or “transferable security”		X				
Rules set out in the UCITS Directive pertaining to the valuation of assets and the rules for calculating the sale or issue price and the repurchase or redemption price of the units of a UCITS, including where such rules are laid down in the applicable national law, in the fund rules or in the instruments of incorporation of the investment company;		X				
UCITS Directive rules on the arrangements for the identification, management and monitoring of the conflicts of interest, including between the management company and its clients, between two of its clients, between one of its clients and a UCITS, or between two - UCITS;		X				
UCITS Directive provisions pertaining to the requirement to appoint a depositary, safe-keeping and the requirements of the depositary, as applied to security tokens;		X				

Disclosure and reporting requirements set out in the UCITS Directive		X				
Other						

Please explain your reasoning (if needed):

Eligibility of assets – GDF notes that Article 50 of UCITS V specifies the types of holdings permissible within UCITS, including certain derivatives and units in other collective investment schemes. UCITS cannot invest directly in utility tokens or cryptocurrencies, as neither of these fit within the categories defined by Article 50. This creates challenges to the development of a market for UCITS operating in the crypto-asset space.

Valuation of assets – see above.

UCITS depositary – see above.

Definition of UCITS – GDF highlights that Article 1 of UCITS V explicitly defines UCITS in relation to investment in transferable securities, as defined by MiFID II, or other liquid financial assets. To the extent that a fund were to invest in security tokens, that definition would not, in itself, appear to preclude its authorisation under UCITS V. However, for this to be possible, the trading venues (i.e., crypto-asset exchanges) through which the fund were to invest would have to become authorised as regulated markets or MTFs, as defined by MiFID II and discussed in Part II.

Divergent regulatory approaches – GDF highlights that regulators at national level are imposing restrictions on retail clients investing in instruments referencing crypto-assets.