COMPETITIVENESS AND RESILIENCE OF EU INFRASTRUCTURES

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The path toward a more integrated and resilient EU financial sector

More integrated, efficient and resilient European financial market infrastructures (EU FMIs) are the cornerstone of a strong EU financial sector. Hence the efforts deployed to keep FMIs and their regulations tuned to market demand and evolving practices and risks.

This holds true in particular for the FMIs operated by the Eurosystem, with the consolidation of TARGET2 and TARGET2-Securities under a single environment, planned for November 2022. This milestone will be followed one year later by the launch of the European Collateral Management System, a unified platform for managing assets used as collateral in Eurosystem credit operations. By providing synergies, more efficient processes and allowing for optimised liquidity management across TARGET Services, these key projects aim at enhancing EU FMIs in the broad sense.

In the years to come, further steps will have to be taken to help improve the integration, resilience and competitiveness of our market infrastructure sector.

First, market integration and settlement efficiency should benefit from the proposal in March 2022, of the European Commission refit for the Regulation on improving securities settlement in the EU and on central securities depositories (CSDR). CSDR refit will notably provide awaited simplifications on passporting and clarifications on the settlement discipline regime.

Second, the financial sector resilience should be enhanced through a comprehensive approach to cyber threats via the adoption this autumn of the Digital Operational Resilience Act (DORA). By promoting high cybersecurity and operational resilience standards across the EU financial sector, DORA will strengthen the resilience of each actor and reinforce the stability of the financial sector as a whole against the background of a continuous increase in cybersecurity risks. Of major importance in this regard is the introduction of a direct oversight of third-party entities, such as cloud service providers, that will be identified as "critical" for the EU financial sector.

Integrated, efficient and resilient European financial market infrastructures should be the backbone of a strong EU financial sector.

Strengthening the resilience of EU FMIs will also build on information-sharing initiatives, bringing together public authorities, market players and intelligence providers to build joint experience and expertise on cyber threats. At the EU level, TIBER-EU has been developed to this aim; the Euro Cyber Resilience Board (ECRB), a forum for strategic discussions, has been set up in order to improve collective public-private knowledge of the cyber landscape and foster trust and collaboration, in normal as well as in crisis times.

Finally, market players have shown a growing interest for the tokenisation of financial assets to enhance the functioning of market infrastructures. This creates improvement opportunities but also new challenges that need to be addressed. In this respect, in line with their financial stability mandate, central banks have an important role to play as oversees and service providers. There is in particular the need to avoid the creation of monopoly situations linked to technological silos that could emerge with new ecosystems based on distributed ledger technology (DLT) and to prevent regression in the use of central bank money for wholesale transactions.

The Regulation on a Pilot regime for market infrastructures based on DLT, entering into force in March 2023, will appropriately help address these issues: by temporarily granting specific exemptions from existing rules, it will allow multilateral trading facilities and central securities depositories, for a period of up to 6 years, to test the DLT for financial markets and post-trade activities, while ensuring a safe asset tokenisation. However, the Pilot regime would be safer and more efficient, from an exploratory point of view, if access to wholesale CeBM – the safest and most liquid settlement asset – were also provided under a tokenised form.

The Banque de France's wholesale CBDC experimentation programme could serve as a basis for the experimental issuance, at Eurosystem level, of a wholesale CBDC designed for the Pilot regime.

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Progress and challenges in the securities post-trading ecosystem

The Eurosystem has always emphasized the need for harmonisation and standardisation in the EU-post-trading space to achieve further integration, efficiency and resilience. One practical example for this is the TARGET2-Securities (T2S) harmonisation agenda in the context of the work of the Eurosystem's Advisory Group on Market Infrastructures for Securities and Collateral (AMI-SeCo), which has driven harmonisation activities regarding e.g. corporate actions, ISO20022 adoption, as well as legal issues.

In the field of collateral management, major progress has been made since 2019 across European markets in the definition and implementation of the Single Collateral Management Rulebook for Europe (SCoRE) standards. The introduction of Eurosystem Collateral Management System (ECMS) will be another milestone and demonstrates that the Eurosystem has the capacity to drive harmonisation also from within its own central bank operations.

Enabling greater and more fluid movement of payments, securities and collateral across Europe is a key factor in optimizing market participants' liquidity management and allowing them to centralise their liquidity in central bank money. Thus, the ECB supports the call from the market for minimising liquidity fragmentation in the euro area and for creating a single pool of EUR central bank liquidity efficiently available for settling securities transactions, but also for collateral mobilisation and retail and wholesale payments. The T2-T2S consolidation project, which is scheduled to be finalised in November 2022, includes a Central Liquidity Management (CLM) tool, which will allow participants to steer, manage and monitor central bank liquidity across all TARGET Services.

At the same time, there is still significant room for improving efficiency and integration between CSDs and other stakeholders of the securities trading, clearing and settlement ecosystem.

First, there needs to be more competition between CSDs for issuers and for investors/CSD participants.

Second, full ISO20022 adoption in the securities and collateral management space, leveraging global standards for transaction and entity identification and further improving access to central bank money settlement are vital to make the CSD landscape more competitive.

The use of new technologies should not diminish the focus on further harmonisation in post trading.

Third, remaining fragmentation, in particular in the processing of corporate actions and tax, should be eliminated by further harmonisation and possibly also legislative efforts. In this context we are also looking at the European Commission's Capital Market Union agenda to provide further impetus to the existing market harmonisation efforts from the regulatory side.

Besides the harmonisation efforts, digitalisation and transformative financial technology are key drivers in the development of the EU post-trading space. The Eurosystem maintains an ongoing dialogue and analysis with market stakeholders on the benefits and risks of using new technologies in payments and securities infrastructures.

One aspect of such analysis is assessing the scenario of making central bank money settlement available via new technologies such as distributed ledger technologies (DLT). These could one day be introduced in the securities ecosystem if it leads to a material increase in efficiency without compromising safety and security, i.e. any undue introduction or increase of operational or other types of risks.

The Eurosystem has taken note of various projects and/or experimentations involving market participants and welcomes these pioneering efforts. Nevertheless, discussions on the use of new technologies should not diminish the focus on further harmonisation of rules and practices to facilitate financial market integration. On the contrary, it may even be the case that more innovation requires more harmonisation efforts to ensure that new competing proposals and models are interoperable and do not re-introduce fragmentation and overall cost increases.

In summary, there are a lot of challenges ahead but there is also encouraging progress. For the Eurosystem operational part, it has been noted that T2S and the TARGET Services in general are becoming a magnet for more EU and EEA markets as exemplified by the formal interest expressed by Euroclear Bank, which signed the T2S framework Agreement at the end of 2021, the Nordic countries Sweden, Norway and Denmark, the planned EUR joiners Croatia and Bulgaria and others who are interested in using the TARGET Services.

We are committed to continue the evolution of T2S as part of the wider TARGET Services, and we aim at making it future proof.

PIERO CIPOLLONE
Deputy Governor - Banca d'Italia

Integrating DLTs with FMIs: challenges, regulation and steps forward

Distributed ledger technologies (DLTs) have great potential for use in securities trading and financial markets infrastructures (FMIs). As in other domains, they are expected to bring significant efficiency gains, thanks to process simplifications, extension of operating times, reduction of costs and times for cross-border transactions and faster security transfers. Greater transparency and traceability will improve control activities. A reduction is expected in both counterparty risks, because of time compression and greater traceability, and operational risks, due to fewer manual activities and the storage of information in decentralized databases. The broader accessibility to investment platforms is expected to facilitate investments too.

However, these benefits could take time to materialize. It will be necessary for: i) DLTs to grow in maturity, containing operational risks and increasing cyber resilience, scalability and sustainability; ii) common standards for DLT platforms to be defined, overcoming interoperability issues; iii) integration with legacy systems of investors to be pursued, until DLTs are able to support the entire transaction cycle; and iv) a complete regulatory framework to become operational, at least at European Union (EU) level. The adoption of DLTs inevitably raises concerns relating to cyber risks, the disintermediation of financial intermediaries (or even central banks), increasing reliance on external providers, and greater liquidity risks until the volume of transactions in DLT platforms consolidates. Governance aspects are also important as, for regulatory and supervisory actions to be effective and enforceable, the identification of accountable entities is needed. All this could undermine the smooth functioning and efficiency of financial markets.

As regards DLT-based Financial Market Infrastructures (FMIs), up until now, business cases have been unable to gain much momentum. This is also due to the lack of a harmonized legislative framework, capable of guaranteeing and promoting initiatives in that direction. An important stimulus in the EU is provided by the recently introduced Regulation on a Pilot regime for FMIs based on DLTs. This regulation allows FMIs to experiment with the supply of trading and settlement services for financial instruments using the DLTs, through the temporary exemption from some regulatory requirements. It aims at promoting innovation while ensuring investor protection, market integrity and financial stability. However, it is not yet sufficient. At national level too, it is necessary to create essential legal prerequisites allowing operators to issue and circulate native digital securities. In Italy, legislative regimes are considering relaxing legal requirements, requiring minimum criteria for DLT technologies, and defining a monitoring regime for DLT-based products and services.

DLTs in financial markets could bring significant efficiency gains and facilitate investments.

Another element that could contribute to the adoption of DLTs in financial markets would be the availability of a Central Bank Digital Currency (CBDC), which could facilitate the use of a comprehensive Delivery vs Payment (DVP) approach in a DLT framework. In the absence of a Eurosystem service to settle the cash leg of DLT transactions in central bank money, market players could turn to other means of payment, such as commercial bank money or stablecoins.

An alternative approach would be a 'trigger solution', which is a component for integrating DLT platforms with existing Eurosystem market infrastructures. Because it relies on existing infrastructures, a trigger solution would be characterized by shorter time and lower costs of adaptation for the Target services, compared with a completely new DLT-based CBDC. Indeed, as noted above, DLT technology does not yet appear to be sufficiently developed for an extensive application in euro-area financial markets. Furthermore, the use of the trigger solution would reduce the risks of fragmentation of the liquidity needed for the cash-side of the settlement systems and would considerably reduce the risk of an impact on Eurosystem market infrastructures, in particular on T2S, a fundamental milestone in the integration of the European securities market.

In this regard, Banca d'Italia has just published a paper[1] on a trigger solution centred on the Eurosystem's TIPS instant payments platform. This solution builds a bridge between DLT platforms, where digital securities are issued and circulated, and the Target services, where central bank money settlement takes place. This Banca d'Italia model provides a DLT-agnostic API to synchronize the asset-leg and the cash-leg, making an instantaneous DVP transaction possible on a 24/7 basis. The paper also reports the results of experimental activities conducted with Algorand, one of the most advanced blockchain for the financial sector available on the market.

[1] https://www.bancaditalia.it/pubblicazioni/mercati-infrastrutture-e-sistemi-di-pagamento/approfondimenti/2022-026/index.html?com.dotmarketing.htmlpage.language=1.

JULIAN REISCHLE

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Capital Markets Union: the next steps of a collaborative initiative

The Deutsche Bundesbank, as an integral part of the Eurosystem, has always been a driving force in advancing both the post-trading landscape and payment systems. We are part of a consortium of central banks that successfully built T2S, operates it smoothly, and is developing it further with the upcoming TARGET2/T2S consolidation project. However, Eurosystem projects can only reach their full potential if they are supported by harmonisation and legislative initiatives. The Capital Markets Union (CMU) is ultimately not an infrastructure project, but a multilevel integration of capital markets within the European Union. While the Eurosystem is always willing to play its part in the integration of capital markets in Europe, it must certainly be accompanied by legislators and market actors.

A prime example from the recent past is the Shareholder Rights Directive II. While T2S made cross-border settlement easier, it alone did not guarantee that investors could also exercise their rights as shareholders. The financial industry itself did not have any incentive to facilitate this, especially for retail clients because it is costly and rarely are clients actively asking for it. For this reason, European legislators had to step in and propose the Shareholder Rights Directive II, which compelled intermediaries to reconsider. Ultimately, it was these intermediaries that developed the standards and processes that enabled the interaction between investors and listed companies.

European legislators seem to be swifter than the Member States when it comes to forcing private actors to contribute to the CMU. However, the next step should be EU-wide harmonisation of withholding tax procedures. Taxation is considered an obstacle to the integration of capital markets due to the lack of harmonisation between national legal systems. Different withholding tax procedures may discourage cross-border investment if taxes are paid in both Member States (of the investor and the investment) and can only be reclaimed via bureaucratic procedures. This mechanism is burdensome and expensive in terms of time and resources and clearly has a negative impact.

CMU is not an infrastructure project, but a multilevel integration of capital markets within the EU.

While doing more may be warranted in some circumstances, doing less is the right choice in others. We therefore welcome the European Commission's proposal to review the CSDR, which would pare down the mandatory buy-in regime. In its original form, this was too complex to implement and placed unnecessary burdens on the non-failing trading partners. In the published proposal, the regime would be eased significantly and activated only in specific circumstances. This guarantees that this policy instrument remains part of the toolkit and can still act as a deterrent to reduced settlement efficiency by market participants. Similarly, we welcome the simplified CSDR passporting process and the revision of the rules concerning CSDs' access to banking-type ancillary services.

The launch of the European Collateral Management System (ECMS) and the accompanying harmonisation initiative to establish a Single Collateral Management Rulebook for Europe (SCoRE) next year is a yet another example of the Eurosystem going hand-in-hand with the financial industry to take the opportunity to advance the integration of EU financial markets. The existing national collateral management systems of the NCBs currently used in the context of collateralising Eurosystem monetary credit operations will be replaced by the ECMS, but the accompanying push towards harmonisation goes far beyond this and will simplify the cross-border handling of collateral in Europe.

A real game changer for the European capital market would be a central bank digital currency (CBDC), either a retail or wholesale version, as a digital form of a truly European means of payment. It would serve as a monetary anchor and support European sovereignty in the landscape of digital payments. In particular, it could enhance the settlement of future digital securities. Past experiences also hold true here: collaboration and the appropriate amount of action by the central bank are crucial. The Eurosystem does not strive to abolish the two-tier banking system, but intends for it to continue to form an integral part of the future payments landscape. Striking the right balance is difficult, especially when large-scale experiments are not really feasible.

The Eurosystem's High-Level Task Force on CBDC is investigating several options for how a digital euro could be designed and it has an intensive outreach programme to both professionals and everyday consumers in order to better understand their needs when it comes to digital payments.

It is too early to say what the solution may be, but it is clear that, as is so often the case in post-trading and payments, its success will depend on the joint effort of the Eurosystem, financial institutions, regulators, and legislators.

ILSE
PEETERS

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Securing the achievements of the EU CSDs' ecosystems while innovating – a call for pragmatic progress

A lot has been written and said regarding the EU CSD landscape over the last 20 years. The Giovannini reports marked the start of a well-known journey that took CSDs from a Code of Conduct on Clearing and Settlement to Target2Securities, the CSDR and its implementation (until even very recently with the settlement penalties), and numerous harmonisation efforts, including in the area of collateral management in the frame of the Eurosystem Collateral Management System (ECMS). Today, the European Commission proposal on CSDR REFIT is being discussed. We welcome the REFIT proposal which is designed to cut red tape and make the cross-border provision of CSD services easier.

It is now time for reflection on (i) the achievements of CSDs, (ii) realistic avenues for further progress in this area and (iii) expectations on how technologies such as DLT can help CSD's and their ecosystems to progress.

First, the achievements in the CSD area are numerous and successful. CSDs have weathered several recent challenges such as Brexit (with the successful migration of Irish corporate securities to Euroclear Bank), numerous COVID19 impacts including dealing with very high levels of volatility, the issuance and distribution of new debt securities such as SURE and NGEU, implementation of Russian sanctions. In all these circumstances, CSDs have served issuers, investors and their agents well. CSDs have proven to be true safe and resilient havens.

Second, we still hear and appreciate there are expectations that further integration or even consolidation amongst CSDs should be the end goal. Conceptually, this expectation makes sense, as some activities of CSDs represent sizeable economies of scale and further integration would allow to reap more synergies and hence increase efficiencies both for domestic and cross-border activities. Yet, a pragmatic approach must be taken in the current EU political environment. Experience tells us that Member States in particular do not see further harmonisation of crucial elements (such as securities law harmonisation and withholding tax procedures) as a priority. Also, very often, Member States understandably consider their CSD of domestic critical importance. Other elements that render further integration challenging are the existence of different holding models within EU CSDs as well as the fact that there are multiple currencies in the EU. Those realities make that progress in the CSDs' ecosystems will continue to take place at an incremental pace.

New technologies, in particular DLT, hold a promise for capital markets and CSDs' ecosystems.

Third, at the same time, we see new technologies, in particular DLT, inherently hold a promise for capital markets, and for the CSDs' ecosystems in particular. Some of the benefits DLT could bring are a reduction of the reconciliation workload between intermediaries, facilitation of the identification of end-investors and the management of registers, a reduction in the trading settlement cycle, etc.

DLT, because of these potential promises, has been attracting a lot of attention from the market over the last few years and has led to many experimentations, including the central bank digital currency pilot with the Banque de France and we have also seen some real life implementations. From those experiences, we can conclude it is probable that DLT could be effectively introduced in the capital market processes in the coming years. Uncertainties however remain on the pace, scope and extent of these upcoming changes.

DLT is not the panacea that will resolve all market problems. Indeed, DLT will initially add complexity to the capital markets that was built around non-DLT systems over the past decades. In addition, some elements that are not harmonised at EU level will need to find their way into the DLT implementations, making them a possible source of fragmentation or additional costs. For example, entities that want to enter the Pilot Regime for DLT Market Infrastructures will have to adapt to different national laws on digital assets which may even not be available yet in all Member States.

A move to a DLT environment without having gained sufficient maturity on its potential impacts may bring the EU capital markets backward rather than forward. Thoughtful and measured pace must be ensured. We therefore support the recently published regulation that designs a DLT Pilot Regime. This should allow for an environment where we can analyse the possibilities and complexities of the implementation of this new technology for trading, settlement and custody of digital assets, answering questions like, what are the more suitable solutions with regard to the cash leg of DLT settlement, and what could be possible market re-shaping that would be warranted.

The above arguments demonstrate how critical it is to have a regular and open dialogue between the public and private sector to understand and support the evolving CSD environment with the aim to bring most benefits to EU's capital markets.

DANIELA PETERHOFF

President of Clearing and Head of European Markets Strategy - Nasdaq

Resilience, efficiency, competitiveness: finding the right balance!

Post-trade infrastructures are often referred to as the plumbing of financial services, suggesting they are highly complex and a bit secondary while in fact they are tremendously important, not least for financial stability. Without them markets cannot function successfully! Looking at CCPs, one can only be impressed by the resilience and containment effects that CCPs brought to financial markets during the global financial crisis. The same holds true for the way market infrastructures navigated through the exceptional market conditions that emerged during the COVID pandemic and more recently because of the invasion of Ukraine by Russia.

CCPs control of markets dynamics are in big part due to the stringent common regulatory requirements that EMIR created as well as its successive refinements imposed to CCPs throughout the EU, including to manage Brexit. Effective supervision, now coordinated by ESMA CCP Supervisory Committee, is also playing an important role there. Nonetheless, I would like to underline that CCPs have worked tirelessly to implement these standards, leading to robust risk management frameworks across the board as suggested by the very encouraging results of ESMA´s fourth stress test.

And, as we cannot rest on our laurels, just a few months back the European Commission carried out a targeted consultation on the review of the central clearing framework in the EU, asking the industry to reflect on several important topics, including the attractiveness of CCPs.

Nasdaq naturally contributed to this exercise and welcomes all the reforms and requirements that make post-trade infrastructure more resilient and prone to support stability. At the same time, a part of me also thinks that all these requirements and changes to implement come at significant costs for the infrastructure themselves and the broader industry with consequences on competitiveness. First, I have in mind the competitiveness in the EU markets, vis-à-vis Over-The-Counter markets for instance, and internationally, vis-à-vis third country markets.

Policy makers therefore need to keep both aspects of resilience and competitiveness in balance.

For me, the reality we must face is that being reliable, resilient, sustainable is not sufficient for post-trade infrastructures. It is not worth very much if such infrastructures end-up not being used because of a lack of competitiveness. The right balance needs to be struck between requirements imposed for resilience and stability purposes and allowing infrastructure to remain competitive in the EU markets as well as globally. For instance, in commodities markets, such as European power markets, a trend has emerged whereby market activity is moving to over-the-counter, away from organized markets and central clearing because their requirements are becoming too burdensome. This development deters the resilience, stability, and sustainability of the markets.

There are also new challenges ahead of us where we will need to stay in balance between too heavy requirements and keeping post-trade market infrastructure competitive. This is especially true in the areas of new technologies, such as DLT and AI but also climate change. Given we see these sectors as essential for society in the future, adopting the adequate frames to facilitate their uptake and monitoring their development is hugely relevant for us and an integral part of Nasdaq strategy.

Whether it is the creation of new types of financial and non-financial digital assets, inventive ways of structuring clearing services using technology to disintermediate or to rethink the status-quo of the traditional trading-clearing-settlement-custody divide in the chain of transacting and holding a financial instrument, policy decisions will have to be made to ensure safe while competitive market solutions. Nasdaq is embracing these new technologies as they have the potential to create more competitive and agile markets and services, while at the same time recognizing the need for ensuring a level playing field between various service providers based on the principles of a technology neutral regulatory framework. The other side of the coin is also that these new technologies can facilitate developments in market infrastructure by putting in place even more effective controls and managing complexities more effectively than today´s markets, allowing even more resilient and orderly markets in the future.

We also need to understand how climate change could pose risks affecting the financial markets including post-trade infrastructures, especially CCPs, and determine an adequate regulatory framework. While ensuring the resilience of markets by posing regulatory requirements on the market infrastructure, it is important to maintain their attractiveness by keeping the demands reasonable.

Importantly, post-trade infrastructures need to be both truly competitive and resilient for remaining efficient and attractive. Policy makers therefore need to keep both aspects of resilience and competitiveness in balance to ensure an efficient and sustainable European capital market!

HAROUN BOUCHETA
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CMU: next regulatory challenges to boost the EU post-trading area

Since the first Giovannini Report from 2001, we know that in order to promote an efficient functioning of EU post-trade markets and to develop cross-border transactions some barriers should be removed.

Significant progress is about to be made with regard to the capital markets union (CMU). The second action plan dated 2020 includes renewed policy objectives which take into account not only the sources of inefficiency notably in the post-trading area but also political developments such as Brexit. Public policy objectives have therefore been redesigned with a balanced approach mixing items like the need to decrease costs and to promote an open EU market with the need to encourage a strategic autonomy.

Having in mind these policy objectives and focusing on the post-trading area, four paths may be followed in order to integrate national capital markets into a genuine single market.

1. "Quick removal" of some technical issues to create a more integrated EU capital market

- Review of the shareholder rights directive (SRD II) through a dedicated regulation aiming at harmonising the definition of shareholder so that cross-border investors are able to exercise their voting rights and their intermediaries can be subject to clear and harmonised rules across the EU,
- Introduce a common EU-wide system for withholding tax to simplify the process for cross-border investors and their intermediaries. It is now time to move forward through political will despite the fact that tax issues should usually be tackled at Member State level,
- Stabilise the settlement discipline regime through the targeted review of the central securities depositories regulation (CSDR) avoiding imposing unnecessary burdens on market participants. Mandatory buy-ins could hurt liquidity and negatively impact the competitiveness of European capital and post-trade markets.

Achieving a genuine post-trade market implies to move quickly on a number of regulatory priorities.

2. Meeting the "strategic autonomy" objective while ensuring a fair competitive landscape

For legitimate reasons, the Commission would like that EU clearing members and market participants reduce excessive exposures to systemically important UK central counterparties (CCPs) in particular for their euro-denominated OTC derivatives exposures. Maintaining a fair competitive landscape is key and any policy that would only involve EU-based clearers will damage those firms and their clients. Punitive capital charges targeting EU banks only would not meet the CMU objectives. Regarding exposures to UK CCPs, the only valid way is to promote policy measures preserving the competitive landscape and including reasonable conditions and timeframe.

It is clear that it is a common interest to maintain liquidity and efficiency benefits of CCPs – regardless where they are located - through a critical mass of non-EU but also EU clearing members.

3. To decrease costs, market structure should evolve

The review of the markets in financial instruments regulation (MiFIR) is a key component of the CMU action plan. Both the consolidated tape and the open access are building stones that could contribute to the CMU goal.

Firstly, regarding the consolidated tape, it is a fact that there is a lack of access to data at a reasonable commercial cost. Market data should be made available as widely and cheaply as possible. One way to achieve this goal could be to have a consolidated tape which is run as a utility by providing data according to a fee reflecting the cost of aggregation and distribution.

Secondly, regarding open access for ETDs, we think that it is too early to stop discussing especially in a CMU perspective. Open access for cash equity markets spurred competition among financial market infrastructures and lead to an overall decrease of costs. Concerning ETDs there are potential risks and costs associated with open access but there are also potential advantages especially in terms of competition and fees.

4. Ensuring client protection for custody and depositary services including for digital assets

The conditions under which custodians and depositaries provide their services to clients is a key component of the investor protection regime.

On the one hand, under the draft review of the directive on alternative investment fund managers (AIFMD), national competent authorities may be allowed to authorize AIFs to appoint a depositary in another Member State. Given the lack of harmonisation of national rules and supervisory approaches applicable to both AIFs and depositaries, it is important for investor protection to limit this possibility and to clarify rules applicable regarding both the supervisory requirements and the duties of depositaries.

On the other hand, the regulation on markets in crypto-assets (MICA) has made clear that custodians will play an important role in this market appropriately accompanying issuers and promoting a secured crypto-assets market. That is why their liability regime should be well calibrated to protect investors but also to encourage players to engage in this new market.