Blockchain for Europe
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BC4EU Response to EC consultation on integration of EU capital markets

General comments

Distributed Ledger Technology (DLT) has the potential to fundamentally transform the types of financial products available and the infrastructure that supports them. The benefits of tokenisation have been well documented, but they can be summarised as follows:

- Market efficiency gains: the automation of processes could remove the need for intermediated activities that add frictions to the asset trading life cycle, therefore streamlining operations and reducing costs.
- Transparency gains: DLT provides an immutable record of transactions and ownership. While complete transparency in all financial transactions might be undesirable and indeed there are market based solutions to build privacy in public blockchains, in some cases it can support price discovery by making information more accessible to market participants and reduce information asymmetries in certain markets.
- Liquidity and tradability: tokenisation may enable broader retail participation in capital markets through fractional ownership of assets. It could also help unlock liquidity for a wider range of previous illiquid assets.
- Settlement efficiency: tokenisation allows for near real-time settlement, reducing counter party risk and potentially freeing up capital.

These innovations closely align with the objectives of the European Savings and Investment Union (SIU) and indeed previous efforts to build a fully integrated CMU. However, in order to propel this vision forward, tokenisation should not be seen as an isolated priority, but as a vector towards a fully digital markets union.

DLT Pilot Regime: shortcomings and potential opportunities

While the EU's current DLT Pilot Regime represents an important first step in promoting broader adoption of DLT in capital markets, it has struggled to take off as initially envisioned. A number of factors have limited its potential, some of which are practical and others which are conceptual. At a practical level, the restrictive thresholds, scope of asset classes, market participants and expiration dates have limited the potential for commercial viability and therefore the incentives for participation. At a conceptual level, this regime seems to have been designed with incumbents, rather than new entrants, in mind. As such, its focus is on amending the existing regulations rather than developing a bespoke framework for DLT.

Aligning the EU's vision with that of other competitive jurisdictions

We believe that the most effective and ambitious path forward is to transform the DLTPR into a permanent waiver-based framework, similar to what other competitive jurisdictions have done. This

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would give regulators the flexibility to permit specific exemptions to legacy financial infrastructure rules where equivalent outcomes can be achieved via DLT-based systems and therefore promote incumbent participation. For new entrants, this should be accessible without obtaining existing licenses, which were designed to address risks posed by legacy infrastructure and functions.

This approach also alleviates the need for a structural revision of the existing EU financial framework and better accommodates rapid technological innovation. In fact, this follows the exact model envisioned by the European Commission when it introduced the DLTPR and recognises that there is still very limited practical evidence of use of DLT in capital markets since only a few entrants have actually entered the pilot and no meaningful evidence has been gathered.

Reforming the regime risks codifying constraints that may not reflect actual market behaviour or risk. In the meantime, empowering ESMA with an enhanced coordinating role would reduce fragmentation and prevent regulatory arbitrage between Member States, ensuring consistent supervisory standards across the Union.