



Blockchain – Legal framework & practical aspects

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I. MAIN AIMS OF BILL 7637

Main aims of Bill 7637

- Past legislative initiatives:
 - Securities Act 2001 was amended to enshrine the use of DLT devices to settle fungible securities.
 - However, the DLT **issuance step** was missing.
- Aim is to modernise the framework of the Dematerialised Securities Act 2013 and to tweak the Banking act 1993.
- Main aims:
 - Issuance account for dematerialised securities can be kept or held via a DLT (such as Blockchain).
 - Opening the role of central account keepers to Luxembourg and EU credit institutions / investment firms for unlisted debt securities.
 - Not to create a fourth class of securities.

Main aims of Bill 7637

- New regulation on Markets in Crypto-assets (MiCA) and proposed directive to amend MiFID II:
 - Regulation goes in the right direction.
 - Focus of the regulation on crypto-assets that are not covered by existing legislation as financial instruments.
 - ➡ Whether or not it is applicable depends on the content of an instrument and not on the technology that is used to issue it ('substance over form').
 - Refinements to be found for the scope of security tokens (particularly unlisted debt securities).
 - Actors in the DLT space will be regulated.
- Bill 7637 is not at odds with MiCA and the proposed directive to amend MiFID II (for now).

II. CENTRAL ACCOUNT KEEPER ROLE

Central account keeper

- Entities currently eligible for acting as central account keeper:
 - Settlement organisation (Art. 1, 6) of the 2013 law on dematerialised securities).
 - Central account keepers (Art.28-12 (1) of the 1993 law on the financial sector):
 - ➡ Luxembourg credit institutions
 - ➡ Luxembourg investment firms
 - ➡ Luxembourg branches of EU credit institutions
 - ➡ Luxembourg branches of EU investment firms
- Bill of law 7637: Opening of the activity to certain entities for certain types of securities:
 - EU credit institutions and EU investment firms.
 - Limitation to unlisted debt securities.
 - Conditions to be met for the provision of the activities by EU credit institutions and EU investment firms.

Central account keeper

- Conditions to be complied with by Luxembourg central account keepers (Art.28-12 of the 1993 law).



Adequate professional experience of management

Robust internal governance arrangements

- Common conditions to be complied with by both existing and new actors:

Control and security mechanisms of IT systems adapted for the keeping of central accounts allowing:

- the registration in an issuance account of all the securities composing each issue admitted to their transactions,
 - the circulation of securities by transfer from one account to another,
 - the verification that the total amount of each issue admitted to their transactions and registered in an issuance account is equal to the sum of the securities registered in the securities accounts of their account holders and
 - the exercise of the rights attached to the securities recorded in the securities account.
- The issuer's administrative bodies are responsible for choosing the settlement organisation or central account keeper (Art.7 of the 2013 law).

III. ISSUANCE ACCOUNT ON DLT LEDGERS

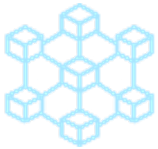
Issuance account on DLT ledgers

- Issuance account is used as the primary account to initially record dematerialised securities. The inscription of dematerialised securities in the issuance account **serves to record** the creation of the dematerialised securities.
- The amendment to the Dematerialised Securities Act 2013 aims to **expressly recognise the possibility to use DLT technology** to record the **creation of unlisted and listed dematerialised securities** (broad definition for the term of “securities”).
- The issuance account would then be operated directly on DLTs (in the form of an issuance wallet or other).
- Issuance account would serve as the primary register: no more need to have two separate registers, a ‘physical’ one and a ‘DLT’ one.
- This amendment would then allow for an *ab initio* issuance of DLT securities.

IV. PRACTICAL CONSIDERATIONS

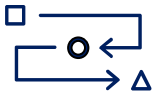
Practical Considerations

In addition to the need of regulatory certainty (Bill 7637), operational considerations are key to the development of DLT Securities issuance projects by regulated stakeholders:



The operating model of the DLT Securities issuance, between decentralised and centralised governance:

- How to issue DLT Securities in a compliant way (KYC/AML/Embargos & Sanctions)? Whitelisting, oracles...
- How to settle the tokens? Commercial money in token form, CBDC, stablecoins...



Main structuring options for the issuance of DLT Securities:

- Public and private blockchains
- Native vs non-native DLT Securities / Listed vs unlisted DLT Securities
- Liaising the primary and secondary markets of the issued DLT Securities



The choice of service providers related to DLT Securities:

- Which role for the custodian / central account keeper?
- How to enhance liquidity on the secondary market of the DLT Securities?

Practical Considerations

Financial institutions and market infrastructures together with fintech are already paving the way to the future digital landscape:



The Société Générale group has realised two bond issuances on public blockchain since 2019. On May 14th 2020, Société Générale SFH, the covered bond vehicle of Société Générale, issued €40 million of covered bonds as security tokens directly registered on a public blockchain. Rated Aaa by Moody's and AAA by Fitch, these OFH Tokens were fully subscribed by Société Générale which simultaneously paid the issuer in a digital form of euros issued by Banque de France through a blockchain platform. This transaction follows in the footsteps of an initial issue worth €100 million in security tokens by Société Générale SFH on 18 April 2019, which was settled in the traditional manner in euros. These issuances seal a new stage in the development of Société Générale - Forge platform, aimed at promoting new blockchain-based market activities.



The blockchain-based system enables frictionless collateral swaps. The first live transactions were carried out by Commerzbank, Credit Suisse and UBS on the Eurex Repo F7-trading system. UBS and Commerzbank swapped ownership of a basket of German government bonds and a basket of corporate bonds, with Clearstream Banking S.A. acting as custodian. This was followed by a cross-custodian swap in which UBS and Credit Suisse exchanged ownership of a basket of corporate bonds at Clearstream Banking S.A. and a basket of German government bonds at Euroclear Bank without physically moving securities between the collateral agents.



SIX is building a fully integrated issuance, trading, settlement and custody infrastructure for digital assets. The SIX Digital Exchange (“SDX”) will enjoy the same standard of oversight and regulation by FINMA, as SIX. We will bring security and reliability to the financial ecosystem of tomorrow. Members of the exchange, usually licensed financial institutions will not only be able to trade on public marketplaces but also privately between themselves.

Practical Considerations

- 01 **Legal and regulatory framework is a must have for the business development of Crypto Assets** solutions within Financial Services Industry.
- 02 Based on the current Luxembourg laws and future European Markets in Crypto Assets Regulation (MiCA) and Pilot regime, we will **have a legal and regulatory framework to operate all the current activities of the security and payment value chain** (issuance, register, distribution, exchange, settlement and custody services, as well as advisory and placement services).
- 03 The future regulatory framework (MiCA / DLT Pilot regime) aims to fulfill the legal gaps further to the development of new crypto assets and DLT. It also aims to provide an innovative, risk averse and consumer protected environment. **The new regulations / laws do no aim to replace the regulatory framework** (MiFID, EMIR, CSDR, MAR, CRD, UCITS V, AIFMD, etc....) which have been put in place since 2008 within the financial industry and will prevail also on Crypto Assets which qualify under these existing regulations.
- 04 **The regulatory framework is not only a set of articles and requirements** around crypto-assets (exchange, issuance, etc.) **but also an unique opportunity to innovate and develop around new services** (custody services private key wallet, new DLT markets platform,...) and **financial instruments**.
- 05 The new Luxembourg law as well as the upcoming regulatory framework provide an unique chance and opportunity for **Luxembourg Capital Markets to play a key role in the digital design and transformation of financial services landscape** in Europe and globally.

V. NEXT STEPS

Next steps

- Bill 7637 is still in the process of receiving comments from various industry groups. Outlook is positive.
- Parliamentary vote.
- Stay tuned for the next Webinar where speakers will discuss around the theme:

Digitalization vs. Tokenization
synergy or opposition?

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