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Innovation in the Securities Markets: ESMA Releases Discussion Paper on Distributed Ledger Technologies

The European Securities and Markets Authority (“ESMA”) published today a [Discussion Paper](#) on the application of “distributed ledger technologies” (“DLT”) to securities markets.

This technology derives from the virtual currency market (where it is known as a “blockchain”). A distributed ledger is essentially an asset database that can be accessed by any number of participants with the requisite permission, allowing entries in the ledger to be updated by one or some of the participants, depending on the rules agreed, with security enforced by computer-based encryption.

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ESMA has published this Discussion Paper to assess the possible benefits and risks that DLT may bring widely to the securities, clearing and settlement markets. ESMA identifies the following possible benefits:

- A DLT network would ensure that all participants hold their own copies of the ledger of a particular security with no conflicting information. This would reduce the number of intermediaries involved, speed up clearing and settlement of financial transactions and make the reconciliation process more efficient.
- A DLT network could facilitate ownership records of many types of securities by using existing standard security identifiers (such as the ISIN) and by increasing automation of corporate action processing.
- A DLT network could facilitate the collection of data for reporting and risk management purposes by ensuring access to a large body of information from a single source. It would also greatly assist supervisory authorities to have direct access to ownership information.
- A DLT network could reduce counterparty risk of certain securities transactions, potentially removing the need for central counterparties to intermediate for cash “spot” transactions, because the settlement could be almost instantaneous.

ESMA also refers to a number of key challenges, such as allowing for position netting and corrections to mistaken entries on the ledger. Further work would also need to be done on fitting DLT networks into existing regulation. This is an early step in accommodating potentially revolutionary new trading and ownership systems into the existing EU framework.