Asia-Pacific Financial Forum Developing APEC’s Financial Market Infrastructure: A Roadmap - Presentation

Purpose: Consideration  
Submitted by: ABAC
1. Introduction
Supporting the Cebu Action Plan
A Ten-Year Roadmap for the APEC Finance Ministers’ Process

FOUR PILLARS

FINANCIAL INTEGRATION
- Financing MSMEs
- Financial inclusion / literacy
- Facilitating remittances
- Financial services liberalization
- Capital accounts liberalization
- Asia Region Funds Passport

FISCAL TRANSPARENCY
- Fiscal reforms
- Open Data Initiative
- Exchange of financial account information
- Base erosion profit shifting
- Tax and crime

FINANCIAL RESILIENCE
- Macroeconomic policy
- Disaster risk financing and insurance
- Capital market development

INFRASTRUCTURE
- Knowledge portal
- Standardization of terms and practices
- Maximizing PPPs in infrastructure investment
- Long-term investors
- Urban development
- Regional connectivity

FMI ROADMAP

APIP

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Priorities in 2017 (Capital Market Development)

**Capital Market Development**

### Priorities

- **Capital Markets**
- **Financial Market Infrastructure**

### Initiatives

- **Supporting Asia Region Fund Passport**
- **Capacity Building for Repo / Derivatives**
- **Development of APEC FMI Roadmap**

- **Promote portfolio investments**
- **Develop Deep and liquid markets**
- **Mitigate risk and reduce costs**
The APEC Finance Ministers’ Process and Asia Pacific Financial Forum

Finance Ministers’ Process (FMP)

21 APEC Finance Ministries
Advisory Functions: ADB, IMF, OECD, WBG, ABAC

Management entrusted to ABAC
Coordinated through the Advisory Group on APEC Financial System Capacity Building

Asia-Pacific Forum on Financial Inclusion

Asia-Pacific Financial Forum (APFF)

Asia-Pacific Infrastructure Partnership (APIP)

Financial Infrastructure Development Network (FIDN)

Trade, Supply Chain Finance

Financial Market Infrastructure

Capital Markets

Long-term investors / Insurance

Micro-insurance / Disaster Risk Finance
The structure of the recommendations

1. The Roles of Financial Market Infrastructures in the Region

2. APEC Roadmap on Financial Market Infrastructures: Process and Instruments
   - 2-1. Securities Markets: Post-Trade Ecosystem
   - 2-3. Increasing Market Efficiency: Issues Specific to Repo/Lending
   - 2-4. Increasing Market Efficiency: Issues Specific to Derivatives
   - 2-5. Fund Services

3. APEC Roadmap on Data Management and Technology
   - 3-1. FMI Fintech
   - 3-2. Disruptive Technologies / new FMI-like entities
APFF Symposium held in Seoul in April 2017

More than 60 representatives from public and private institutions discussed robust range of topics in a whole day symposium on 25th April.
2. Recommendations
The challenges post-global financial crisis environment

Potential rise of the costs and fragmentation of markets

Potential reduction of liquidity and depth

Potential rise of cost of raising funds from international capital markets

May slow the growth of the economies
To Support the growth of the economies while maintaining stability through enhanced efficient functioning of the markets

- promoting the cross-border portfolio investments;
- utilizing local currency assets as eligible financial collateral by both FMIs and bilaterally;
- maintaining and broadening access to cross-border money transfer mechanisms providing the required transparency in affordable and meaningful way; and
- incorporating innovative and potentially disruptive technologies.

Help address the potential rise of the costs and fragmentation of markets after the GFC, enhance liquidity and depth, making sure the smaller players’ involvement, and lessen the cost of raising funds from international capital markets.
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1. THE ROLES OF FINANCIAL MARKET INFRASTRUCTURES IN THE REGION

a) Standardization and Harmonization

The roles of FMIs have been under the spotlight after the GFC.

Standardization should not only be considered in technical terms.

but also in terms of industry expectations: e.g. issuance documents.

Recommendation 1a: Responsible authorities are encouraged to support the harmonization of issuance rules and enhancing transparency of securities and tax rules; including targeting professional investors such as financial intermediaries to enable common disclosure language, procedures investor protection rules. To promote this, it is encouraged to collaborate with ASEAN+3 Bond Market Forum which promotes ASEAN+3 Multi-Currency Bond Issuance Framework (AMBIF) to link professional markets in the region, and then apply the experience gained to wider APEC economies.
b) Monitoring the effects of G20 regulatory initiatives

The GFC prompted G20 authorities to bring in a new suite of regulations. Those regulations influence markets by way of extraterritorial effects. Domestic CCPs may not be appropriate for all APEC markets.

Recommendation 1b: Securities regulators and central banks are encouraged to monitor together with the region's market participants the extraterritorial effects of developed economies' rules and consider ways to address this, especially in smaller economies. Smaller jurisdictions are encouraged to carefully consider global policies and international best practices and their appropriateness for smaller markets, subject to their size and level of development. They should strive to achieve the outcomes that have been internationally agreed – but be very mindful of what implementation means for their jurisdiction. In any case, the implementation must avoid creating further fragmentation. It should be noted that domestic CCPs may not be appropriate for all APEC markets, but uncleared margin should only be promoted for jurisdictions that have good netting and collateral status.
1. THE ROLES OF FINANCIAL MARKET INFRASTRUCTURES IN THE REGION

c) Measuring the scarcity of High Quality Liquid Assets

- Post-GFC regulations and rules are forcing financial transactions to be further collateralized.
- There is a scarcity of High Quality Liquid Asset collateral.
- Local currency collateral, incl. highly rated gov’t bonds, is often not accepted internationally.

Recommendation 1c: Responsible authorities are encouraged to collaborate together with international organizations, to have workshops to better understand the issues to address the growing need for HQLA collateral in the region. Measures could include how local currency assets could be utilized as part of collateral accepted for cross-border trades between financial intermediaries and CCPs, how regional financial integration and better hedging markets would assist further liquidity, and identification of specific classes of securities where liquidity and eligibility could be expanded; followed by advocacy efforts in jurisdictions where collateral eligibility could be expanded. In this regard, CSD-RTGS Linkages under CSIF of ABMI can be considered as a leading example.
**1. THE ROLES OF FINANCIAL MARKET INFRASTRUCTURES IN THE REGION**

**d) Infrastructure inter-operability and interconnectedness**

FMIs should be encouraged to cooperate in a similar manner to how central banks link to each other.

Not only large value payments and securities settlement systems, but also e-payments need to be interlinked internationally.

Achieving inter-operability may also increase systemic risk from markets becoming more interconnected.

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**Recommendation 1d:** Respective authorities are encouraged to promote inter-operability among FMIs and participants including financial intermediaries, and evaluate the effects of interconnectedness between the markets and their potential impact, implications to policy makers and regulators, measures to mitigate risk while avoiding "risk-off" or hindering financial inclusion.
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2. APEC Roadmap on Financial Market Infrastructures: Process and Instruments

2-1. Securities Markets: Post-Trade Ecosystem

Ecosystem

- FMIs (CCP, CSD, Payments)
- Intermediaries and messaging systems
- Fund services participants

Global and country level new regulatory requirements and implementations

Concern on costs and complexities continue to accumulate

“Behind the border” barriers to cross-border investment

Eventually become significant drain on participants’ growth-oriented investments
2-1. Securities Markets: Post-Trade Ecosystem

Source: Deutsche Bank
2. APEC Roadmap on Financial Market Infrastructures: Process and Instruments

2-1. Securities Markets: Post-Trade Ecosystem

Market access and repatriation requirements

i. New Account Opening
ii. Market Entry and Capital injection
iii. FX Execution and Hedging
iv. Clearing and Settlement
v. Asset Servicing or Corporate Actions and Tax
vi. Repatriation
vii. Reporting

Two possible solutions to address the issues

Greater standardization
Use of FMI as industry utilities (in the process shown left)

A cross-border participant will face the costs and complexities that are amplified by the actual number of activities, the frequency and extent of changes that affect these activities and the number of markets.
2-1. Securities Markets: Post-Trade Ecosystem

Recommendations 2-1

a. For private and public sector collaboration to assess and progress on the regional standardization of account opening documents like KYC/AML and tax reporting that needs to be completed by securities investors who can be domestic or cross-border. Standardization activities will only have meaningful impacts if industry-wide implementation is at the regional level.

b. For regulatory support - for example, through clear guidelines - of the use of 3rd party industry utilities to store, manage and make easy access of such standardized documents ("documentary industry utilities") by relevant parties. For private and public sector to explore the feasibility of such documentary reuse/portability at the regional level and discuss how these goals can be better achieved and in what time frame.
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a) Account structure

Three dimensions:
- asset protection;
- cost; and
- operational efficiency

On a cross-border basis, the omnibus account structure combined with a nominee legal structure is the most effective from an operational viewpoint.

Fixed income assets do not grant ownership rights, which has significant policy implications in terms of national interest and tax purposes.

Recommendation 2-2a: No need to change the way the local market is operating which could be (direct holding, omnibus or a mix of both) but the omnibus is the preferred option for cross-border flows to attract foreign investments to a local market. Both account structures can coexist. Ideally the omnibus account structure should be combined with the nominee concept legal structure.
b) Tax

Consideration from
- Economical perspective
- Operational perspective
  (in addition to fair and equitable)

Investors can request a yield premium to offset a tax rate but will likely not invest or limit activities should the operational complexity be too high.

Firms seek to have a tax regime that does not impose a significant operational burden and that is predictable enough.

Recommendation 2-2b: Prefer no tax or a simple tax scheme (i.e.: a withholding tax based on a Record Date principle), no capital gain tax based on a price difference or a tax calculated on a holding period since they are unmanageable on a cross-border basis. Prefer to tax at source instead of refund. For tax certificates collection, prefer a one-time certificate instead of requiring yearly certificate or certificate per payment. Do not require local notarization of tax certificates.

c) Investor Identification and Transparency

Reason for transparency: statistical, price discovery, KYC, AML, quotas, tax, market surveillance, etc.

Different asset classes are traded differently and bear different risks. -> different treatment

Transparency can be achieved through multiple means; they can be combined.

Recommendation 2-2c: Define the right balance between transparency and market efficiency. Responsible authorities should review whether legal frameworks support requests to report investors’ information and undertake legislative reforms if they do not. Securities regulators and Issuers willing to collect investors information should introduce requirements for bond prospectuses to facilitate such requests. Upon such review, following perspectives are particularly important: (1) Precise definition of the reason for the transparency to ensure the solution addresses the needs and minimizes operational frictions for all involved parties, (2) Ensuring enforceability of investors’ information collection in the law to avoid conflicting regulations between the country of issuance and the investors’ country of residence, and (3) Avoiding the request of data which cannot be automatically retrieved from intermediaries systems or which require interpretation.
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2-3. Increasing Market Efficiency: Issues Specific to Repo/Lending

Benefits of Repo/Lending
- Reduced cost (of investments)
- Improved risk management
- Better liquidity

Challenges of participants
- Monetary Policy
- Capital Account Restrictions
- Int’l Prudential Regulation
- Collateral eligibility
- Short-selling rules
- Disclosure regimes

Public-private initiatives
- Promulgation and promotion of int’l best practices
- Formulation of codes of conduct
- Adoption of international documentation

Viewpoints of Recommendations
- a) Regulatory transparency
- b) Standard documentation
- c) Tax and accounting
- d) Scarcity of HQLA

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2-3. Issues Specific to Repo/Lending

a) Regulatory transparency

Regulatory uncertainty increases market risk and legal risk, which makes the relevant markets less attractive to investors.

If there is an intention to reform certain markets this needs to occur before the end of the global capital market reforms. Once completed, there will be significant resistance for implementing changes, and therefore act as an obstacle to foreign investment.

Recommendation 2-3a: Both responsible authorities and market participants are encouraged to continue to pursue various initiatives, including promulgation and promotion of international best practices and formulation of codes of conduct, to further develop and improve the market, by ensuring very clear principles on regulatory expectations on capital raising and investment.
2-3. Issues Specific to Repo/Lending

b) Adoption of standard documentation

Repo and securities lending market fragmentation is exacerbated by local documentation requirements and standards.

The standard local documentation often does not contain adequate operational details or credit protections for international participants.

Recommendation 2-3b: Securities regulators and policy makers are encouraged to review the local practices if they adopt the international standard documentation such as the GMRA and GMSLA and undertake promotionally initiatives if they do not, including reflecting some locality to be reflected in the standard contract document; e.g. in the form of annex, through the collaborative work with market practitioners and wide variety of stakeholders including industry associations.
Recommendation 2-3c: Responsible authorities are encouraged to support constant dialogues with the industry representatives through public-private platforms including APFF, PASLA, ICMA, Asifma, and ABMF to review current policies and practices could effect as a barrier and undertake reforms if they do.

* Recommendation 2-3d is the same as Recommendation 1c.
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2-4. Increasing Market Efficiency: Issues Specific to Derivatives

Challenges

Post-global financial crisis (GFC) environment

There are many regulatory challenges in trade reporting (explained in later pages).

- lack a true picture of risk in individual jurisdictions because of incomplete and inconsistent trade data

Positive developments

Major jurisdictions have largely implemented their reporting regimes

National regulators are increasingly turning their minds to cross-border efforts

They will require

Active support and cooperation of a range of global stakeholders;

- regulators
- market participants and
- infrastructure providers
2-4. Issues Specific to Derivatives

a) Global convergence on harmonised reporting requirements

Different, costly, duplicative, conflicting and non-standardized reporting requirements across jurisdictions.

Recommendation 2-4a: Shared, public commitment to global convergence on harmonised reporting requirements

Securities regulators are encouraged to review whether their reporting requirements are harmonized, and consistent within and across jurisdictions, and undertake regulatory reforms if they are not.
2-4. Issues Specific to Derivatives

b) Greater regulatory endorsement of data standards and formats already in use

There is a lack of agreement as to how some data reporting requirements should be standardized across jurisdictions. Standardized reporting formats have been not adopted quickly or broadly enough.

Recommendation 2-4b: Greater regulatory endorsement of data standards and formats already in use
Regulators are encouraged to embrace standards for derivatives reporting, and those that have not yet deployed their rules should avoid introducing unique requirements.
2-4. Issues Specific to Derivatives

c) Removal of barriers to sharing information across repositories and borders

Legal barriers exist to sharing data and information, both within and across borders.

Recommendation 2-3c: The removal of barriers to sharing information across trade repositories and borders
Regulators are encouraged to review whether current regulations hinder sharing information across borders, and undertake reforms if they do.
d) Increased availability of substituted compliance

The availability of ‘substituted compliance’ for reporting is limited, adding to duplication.

Recommendation 2-3d: Increased availability of substituted compliance
Regulators are strongly encouraged to defer to each other’s regulatory regimes where their intended outcomes are consistent by adopting equivalence decisions, which allows a multi-jurisdictional reporting obligation for a transaction to be discharged once, in a jurisdiction of the reporting entity’s choice. Regulators with a mandate to access the data for a transaction should obtain that information from that single report.
2-4. Issues Specific to Derivatives

e) Promotion of inter-operability and connectivity between trade repositories

Some reporting regimes are ‘closed markets’ – meaning they have their own trade repositories which do not leverage international standards and mechanisms. They may have unique data architectures, formats and methods of sharing information.

Recommendation 2-3e: Promotion of inter-operability and connectivity between trade repositories
Regulators are encouraged to review the level of inter-operability between trade repositories and promote and incentivise the sharing of data.
2-4. Issues Specific to Derivatives

Recommendation 2-3f: Greater cross-border regulatory focus on global aggregation mechanisms. Regulators are encouraged to leverage cooperation with other authorities to achieve their objectives: both for sharing lessons learnt, as well as sharing data by designating jurisdictional, regional and global leaders to spearhead the aggregation effort.

f) Promotion of inter-operability and connectivity between trade repositories

There is no facilitator or mechanism to aggregate data from different trade repositories globally.
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#### Development of passport initiatives

In an era where more investors can benefit from the diversity of funds offered by fund passport initiatives like the **Asia Region Funds Passport**

#### Challenges of participants

- **Managing the industry costs is important to facilitate these investors’ activities**
- **Some economies still rely on email or other manual process**

#### Initiatives to address the issues

- **Development of funds back-office processing utility**
- **Interoperability among such utilities for cross-border funds**
- **Barriers can be lowered by reduction of complexities**

#### Recommendation

**Recommendation 2-5a:**

Based on the ASEAN CIS experience, securities regulators are encouraged to set highly standardized registration process for funds between passporting economies, in order to ensure that benefits of streamlined regulations are felt by the market. The case of China-HK MRF shows that attractiveness of the product is key in promoting passport scheme, and that large-scale funding for pilot funds received a lot of attention from the industry.
2-5. Fund Services

For the efficiency of fund services

Standardization between business processes will be essential for the automation and efficiency of fund services.

b) Standardization and harmonization

Need for Connectivity

- Fund operators
- Distributors
- Registrars
- Administrators
- Custodians

located in different jurisdictions

without compromising the product’s attractiveness.

Initiatives to address the issues

A consultative body of CSDs was established under the name of Asia Fund Standardization Forum (AFSF) in 2015.

Industry-wide implementation is encouraged on the regional scale.

Recommendation

Recommendation 2-5b: Responsible authorities are encouraged to support for the activities of AFSF. Harmonization can be achieved in many parts of the business process (usage of same fund codes or message formats, required information for fund products by regulators or market players, account opening forms, KYC process, etc.) Standardization in the terminology used between fund markets will be essential for market players to communicate effectively for cross-border transactions.
### Positioning of fund services

Fund services are an integral part of the investment fund business as an infrastructure that supports back-office processing.

### Efforts hindered by

- **Vastly disparate practices**
- **Absence of a market standard**
- **Prevalence of proprietary systems**

### Interesting solutions surfacing

Adoption of centralized fund hubs
- Interconnects the domestic market
- Streamlines the many to many communication between diverse players

**Case:** FundNet (Korea)
**FundConnext (Thai)**

### Recommendation

Recommendation 2-5c:
Regulators are encouraged to support for the development of fund platforms led by infrastructure providers. The recent case of Thailand’s platform is a good illustration of constructive cooperation between the regulator, CSD, and the market.
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## 3. APEC Roadmap on Data Management and Technology

- **3-1. FMI Fintech**
- **3-2. Disruptive Technologies / new FMI-like entities**
3-1. FMI Fintech

a) Know Your Customer

Approximately, 1.5 billion people around the world do not have an officially recognized document to prove their identity.

Classical forms of identity provisioning struggle to reach underserved populations, contain clear security vulnerabilities.

Digital IDs can be linked with electronic forms of know-your-customer (e-KYC) verification mechanisms. API enables private sector match IDs.

Recommendation 3-1a: APEC Finance Ministers and responsible authorities are encouraged to support for the following initiatives of APFF FMI Fintech Substream;

- Conducting a review of the current Digital ID and e-KYC initiatives being rolled out in several APEC member economies
- Analyzing Digital ID and e-KYC initiatives being conducted outside the region to document best practices that could be leveraged within the APEC region
- Focusing its analysis on solutions that are interoperable at least, and harmonized at best, in order to promote economic integration among APEC member economies in Fintech KYC developments.

API: Application Programming Interface
3-1. FMI Fintech

b) E-Payments

E-Payments help to lower transaction costs, increase transparency, and make transfers of money faster and more efficient.

The inter-operability and regulatory requirements associated with payment card solutions and mobile smart phones is currently a challenge for the APEC ecosystem.

There are:
- multitude of players;
- divergence in solutions;
- divergent standards; and
- differences how mobile and card based solutions interact.

Recommendation 3-1b: APEC Finance Ministers and responsible authorities are encouraged to support for the following initiatives of APFF FMI Fintech Substream;
- Exploring whether there are inter-operability concerns that exist in the APEC e-Payments ecosystem and whether APFF can make recommendations on how to resolve those concerns
- Seeking to create a primer on e-Payments in the region
Recommendation 3-1c: APEC Finance Ministers and responsible authorities are encouraged to support for the following initiatives of APFF FMI Fintech Substream;

- Creating a typology of cybersecurity risks in the fintech ecosystem
- Engaging in research and analysis of emerging cybersecurity solutions and share those learnings with stakeholders
- At public-private forums discuss its findings on cybersecurity risks and solutions and advocate how identified best practices can be adopted throughout the APEC ecosystem, without regulatory technology mandates wherever possible

The major vulnerability associated with Fintech is the multitude of new actors it brings into the financial services ecosystem and the linkages created between these new actors.

A cybersecurity ecosystem for APEC can only be as strong as its weakest link.

->interested in creating baseline cybersecurity requirements
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Disruptive technologies provide tremendous opportunities for FMIs and participants to operate more efficiently, better service public and private sectors, increase and simplify access to financial data and products.

The new technology also bring risks:
- technological and operational risks
- fragmentation risks
- cybersecurity and data confidentiality risks
- legal risks, especially for cross-border activities

Recommendation 3-2a: Financial Market Infrastructures should experiment and contribute to the research and development exercise required to overcome the maturity challenge. They should work collaboratively with regulators, the financial industry and the broader public sector. Such collaborative experimentation is important not only to contribute to maturing these technologies further but also to better understand them, ensure focus on the right problems to be solved and identify as well as understand the risks. It also helps getting the necessary buy-in for when an implementation decision needs to be taken.

Recommendation 3-2b: Regulators and FMIs also need to collaborate across markets to agree on harmonized domestic legal frameworks supporting the implementation of such new technologies and ensure cross-border regulatory certainty.
THANK YOU