

READY FOR LIFT-OFF: FRENCH LAW EVOLVES TO BE READY FOR THE EU PILOT REGIME

The EU Pilot Regime (Regulation (EU) 2022/858) came into application today, 23 March 2023. Its aim is to create a secured regulatory sandbox for the creation of distributed ledger technology (DLT)-enabled financial market infrastructures (FMIs) dedicated to digital securities.

These DLT market infrastructures include

- DLT multilateral trading facilities (DLT MTFs);
- DLT settlement systems (DLT SSs); and
- a combination of both (DLT TSS).

For a three-year period, operators of such DLT market infrastructures will be able to apply to be temporarily exempted from certain provisions of CSDR and MiFID II/MiFIR identified in the EU Pilot Regime. The provisions that can be disapplied depend on the type of DLT market infrastructure but the general aim is to allow the applicants to (a) carry out activities using DLT in a way which they cannot do under current legislation and (b) refrain from carrying out activities that are imposed by legislation but are ultimately burdensome or less relevant in a DLT context (For more details about the EU Pilot Regime, please read our Client Briefing accessible [here](#)).

In order to enable international market participants, including issuers, investors and financial market infrastructures, to make the most of the EU Pilot Regime, France has further

Key takeaways

- From 23 March 2023, for an initial three-year period, operators of DLT Market infrastructures will be given the opportunity under the EU Pilot Regime to experiment with the use of DLT in issuance and post-trade processes, free from certain regulatory constraints.
- This is expected to give rise to an increase in the volume of issuances of financial instruments that are issued, recorded, transferred and stored using DLT in Europe.
- Our previous European Capital Markets Client Briefing from September 2022 on the EU Pilot Regime is accessible [here](#).

adapted its existing legal framework for digital securities through the DDADUE Law n° 2023-171 dated 9 March 2023.

France now has a legal framework that is fully compatible with the EU Pilot Regime and provides a clear path forward for market actors looking to use DLT in the primary issuance, secondary trading and post-trade of digital securities in France.

A brief history lesson: from securities accounts to digital wallets

Securities issued in France have been dematerialised since the Dematerialisation Law of 1981. Since then, securities (whether in registered or bearer form) have not been issued in paper-based form and are instead solely represented by book-entries in securities account(s) maintained by the issuer of such securities, regulated financial intermediaries or through central securities depositories (CSD).

Adapting the law to allow for the issuance of securities onto distributed ledgers was therefore far from being a paradigm shift in France. It was simply a case of evolution to allow France to benefit to the fullest extent from the possibilities offered by digital finance. No Schumpeterian revolution was necessary.

Following on from an Order of April 2016 which had allowed for short term notes (*bons de caisse*) to be issued and disposed of using DLT, the Blockchain Order of 2017 allowed unlisted securities to be issued, transferred and delivered on a distributed ledger (known in French as a *dispositif d'enregistrement électronique partagé* or DEEP).

Although the Blockchain Decree of 2018 fleshed out the requirements for the DEEP, digital securities are nevertheless still issued in the same manner as traditional securities in France. In other words, the French securities law framework is adapted for DLT, but has remained technology neutral.

The requirements introduced by the Blockchain Decree for digital securities are the following:

- the DEEP must be structured and set up to guarantee the recording and integrity of the inscriptions and allow for the identification of the owners of the securities, their nature and number of securities held;
- the issuer (or its agent) must have an activity continuity plan in place which includes an external process for periodic safeguarding of data (*i.e.* any entries on the DEEP);
- the owner of the securities registered on the DEEP must have access to a personalised statement of transactions.

No other legal or regulatory requirements are imposed under French law. As a result, in France the DEEP:

- can be a private permissioned blockchain, a public permissioned blockchain or a public permissionless blockchain;
- the DEEP's structure and operations do not require the involvement of a regulated entity. By default, the issuer plays the role of wallet/bookkeeper in the DEEP. That said, this role can be delegated to any third party, acting as the issuer's agent or registrar (as applicable).

As this demonstrates, there is a lot of contractual flexibility given to the parties, which is one of the reasons why French law was selected for the inaugural issuance of digital bonds by the European Investment Bank (EIB) in April 2021.

Creating liquidity through DLT FMIs

Article 3 of CSDR provides that where a transaction in transferable securities takes place on a trading venue, the relevant securities shall be recorded in book-entry form in a CSD. Given that the CSDs are not operationally set up to handle digital securities, and that the legislation governing them is not adapted to their dealing with digital securities either, issuers in Europe have not been able to admit digital securities to trading on regulated trading venues.

The EU Pilot Regime and the development of DLT market infrastructures should therefore be seen firmly in the context of wider efforts to increase the liquidity of digital securities, which have otherwise included the use of bulletin boards and the recently introduced possibility to list digital securities on the Securities Official List (SOL) of the Luxembourg Stock Exchange without admission to trading in order to provide issuers with additional visibility.

Whilst the Blockchain Order of 2017 allowed for unlisted registered securities to be issued onto DEEP, the DDADUE Law has amended French law to allow for bearer securities to be admitted to trading on a DLT MTF and more generally admitted to the operations of a DLT market infrastructure under the EU Pilot Regime. The hope is that this will enable the development of a liquid market for digital securities in France.

Following the DDADUE Law, two options for digital securities issuances coexist under French law:

- unlisted securities, which can be issued, transferred and delivered on a DEEP;
- listed securities, which can be issued, transferred and delivered on a DEEP and also traded and delivered through a DLT market infrastructure governed by the EU Pilot Regime.

Taking collateral over digital securities

Digital securities governed by French law can also be subject to a securities pledge, following minor adaptations made in 2018 as part of the Blockchain Decree to the French legal framework for pledges over securities accounts.

Digital securities can also be subject to a financial collateral under the French insolvency safe harbour.

And what about the cash leg?

The EU Pilot Regime offers some flexibility to perform the cash leg of the DvP process on a distributed ledger by

offering the possibility to use electronic money tokens as an alternative to central bank digital currency. In anticipation for that, the DDADUE Law excludes e-money payments made under the EU Pilot Regime from the cap of EUR 3,000 which applies generally to payments made in e-money.

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