



ISRAEL SECURITIES AUTHORITY

January 20, 2020

RFI on Developing of Digital Capital Markets in Israel

As part of our strategic plan to promote innovation in the capital market, the ISA is working through multiple channels to develop a technologically advanced, innovative capital market that is attractive for both companies and investors. Within these efforts, the ISA is taking steps to promote the adoption of innovative technologies that will improve financial services in Israel, save costs, and enhance the public's access to these services.

To this end, in July 2019 ISA Chair Anat Guetta formed an internal committee to promote digital markets in Israel ("the Committee"). The Committee continued the work of a previous internal committee that examined the regulation of public offerings of decentralized cryptographic assets ("the ICO Committee") and submitted its final conclusions in March 2019. One of the ICO Committee's main conclusions was the need to consider necessary adjustments to existing regulations to create an appropriate regulatory infrastructure for securities-based digital trading platforms (also known as security tokens platforms and digital securities platforms).

The Committee focused on platforms for the issuance, trading, and settlement of securities based on distributed ledger technology (DLT) with a diverse range of properties (e.g., use of tokens and smart contracts). The Committee also conducted discussions and communicated with a large number of stakeholders and regulatory authorities worldwide, from diverse backgrounds, including entities engaged in the business-related and/or technological aspects of setting up trading infrastructure, investors in digital markets, and companies that have already raised or plan in the future to raise capital using digital assets. Following are the main insights that emerge from the current Committee's work.

1. Identifying the Potential

Based on the Committee's extensive review and meetings, we believe that DLT has the potential to promote the Israeli capital market. Adopting this technology may reduce trading costs to end-clients and systemic risks to the economy, and may create a technological environment that encourages financial innovation and increases access to the capital market for

classes of companies (such as SMEs) that refrained from using the public capital market for financing purposes.

In view of the technology's ability to verify and update information that is simultaneously accessible by multiple parties in a rapid, efficient, and reliable manner, the Committee members believe that the greatest added value that might be generated by adopting DLT in financial markets lies in the fields of infrastructure, issuance, and trading (i.e., in registries, settlements, and custodial services).

2. Risks

The use of novel technologies naturally involves risks, especially in the case of technologies that do not yet possess a significant track record in the capital market. Therefore, the deployment of innovative technologies into core systems must proceed in a controlled and responsible manner. These risks should be taken into consideration in developing the ISA's future steps in adopting these technologies, effectively addressing them yet without impeding their adoption.

3. Technology-neutral Approach

It is important that the ISA, like other securities authorities worldwide, maintain a neutral approach regarding the specific technologies that its supervised entities choose to use, provided that these technologies meet the required standards, and their use is not inconsistent with regulatory goals such as prevention of money laundering, investor protection and financial stability. At the same time, the ISA should take steps to remove regulatory barriers that prevent the use of novel technologies that offer added value. Removing such obstacles may also facilitate the adoption of additional technologies that will be developed in the future.

4. Regulatory Considerations

According to the international trends, trading and settlement platforms that became operational rather quickly were those that were established as secondary or alternative trading platforms (such as the Alternative Trading System [ATS] in the United States) by relatively new entities entering the industry. These entrants appear to regard themselves as high-tech ventures seeking to compete with traditional exchanges.

A comparative review of the regulatory regimes in the United States and Europe reveals a regulatory hierarchy of platforms, based on various features, including an exemption on securities exchange licensing requirements that may be issued based on limited trading volumes. In Israel, the licensing and supervisory directives in the Securities Law regarding stock exchanges were shaped by the view that exchanges constitute **significant national**

exchanges that operate through its members. As a result, several of the regulatory requirements that apply to exchanges might impede the establishment of relatively small trading platforms.

The Committee identified additional regulatory issues that arise with respect to the licensing and supervision of such trading platforms, and the ISA intends to examine practical steps to address these concerns.

5. Proving the Benefits of Technology

Many significant benefits have been attributed to DLT, yet these are for the most part theoretical, due to the early stage of DLT adoption in global capital markets. Therefore, alongside work on the regulatory aspects of technology adoption, the ISA should continue to promote studies that prove the added value of the technology, for the ISA and the entire market. Such evidence will join the already existing and extensive information that has accumulated from the meetings and reviewed documents, which might constitute a professional basis for effective action by the ISA.

6. Request for Information

1. In view of the uncertainty regarding the use of DLT, it is not possible to exhaustively identify all the relevant regulatory issues and obstacles. We therefore invite the public to suggest regulatory issues that might arise in promoting markets that use innovative technologies, and specifically might constitute obstacles that impede such development in Israel. Following are several guiding questions:
 - (a) Can you identify provisions in current regulation that are under the purview of the ISA, which might impede the development of a digital market in Israel and especially a market that is based on DLT?
 - (b) Can you identify unique increased risks posed by the use of this technology in the capital market, most specifically risks to securities trading and settlement, which require special regulatory consideration? What are the risks you identified and which aspects of the technology do they involve?
 - (c) Are there any additional use cases that might contribute to the development of the capital market?
2. We invite local and international business entrepreneurs and technology providers to contact us if they wish to:
 - (a) Present or demonstrate a proof of concept (POC) of specific features of DLT relevant for the development of the digital platforms/exchanges, such as legal documentation, issuance, clearing and settlement, custodian, lowering the costs of central depository and registration. You may also consider participating in the pilot

fintech program operated by the Innovation Authority and the ISA. For more information on the pilot program, please see [-Link](#).

- (b) Learn about the relevant regulatory framework in Israel and adjust their operations to the existing requirements (if necessary), and to be guided by the ISA professional team and to benefit from our oversight perspective.

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