

Custody Industry and Regulatory Developments Report

The key regulations, market and industry developments shaping the Custody industry





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Foreword



Hannah Elson
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The securities post-trade landscape is constantly evolving, with impactful regulatory and industry headwinds that require targeted industry engagement and advocacy with regulators, financial market infrastructures and industry bodies to support the custody business, our clients and product strategy globally.

As a leading global custodian, J.P. Morgan allocates significant resources with the objective of harmonising and improving standards in post trade securities services over the 100 markets in which it operates, keeping our clients' interest at heart. The resources are allocated across global custody, direct custody, operations and network management teams, channelling interactions with local and regional regulators, trade associations, market infrastructure and sub-custody network providers.

Our Custody business houses a dedicated team that focuses on regulatory advocacy, including engagement with regulators and industry associations. In close collaboration with internal and external stakeholders, their mission is to ensure that regulatory frameworks and initiatives are focused on a well-functioning, innovative and low risk financial system.

Our participation and leadership in industry trade associations, advisory boards, specific working groups and task forces in addition to collaboration and partnership with our sub-custody and market

infrastructure network enables us to contribute to improving market practices and forthcoming regulation that may affect the firm and our clients.

This is an exciting time in the securities post trade industry with regulatory changes continuing apace, market developments such as accelerated settlement and the emergence of new asset classes and new technologies. This publication intends to give an overview of some of these initiatives and developments that our Custody team are currently advocating for on behalf of our Clients as we engage and influence policy makers, market infrastructures and the wider industry.

It is not an exhaustive list of all the initiatives across the industry which require advocacy, more the key items and themes that we hope you, as our clients, will find useful.

The report is structured as follows

1. Settlement Acceleration
2. Settlement Efficiency
3. Asset Servicing
4. Tax
5. Financial Market Infrastructure
6. Digital Ledger Technology and Assets
7. Regional Developments

Overview

On **settlement acceleration and efficiency**, the move to T+1 settlement has been, and will remain, a key focus as it is fast becoming an important global trend which requires broader consideration of the global implications for our clients, J.P. Morgan, and the securities industry as a whole. We are actively engaged in industry wide discussions on accelerated settlement, and we already have experience in this space having played an active role in India's migration ensuring that market level changes did not have a materially adverse impact on our clients. J.P. Morgan Custody successfully advocated India's regulators and clearing corporations, bilaterally and through our industry association network, for a phased implementation in order to provide sufficient time for our clients to make the necessary changes and also achieving a 12 hour extension to the market affirmation deadline in order to provide sufficient time for our clients to send their trade instructions and make their funding arrangements.

Now with the dates for the U.S. and Canada migrations agreed (28th May and 27th May respectively), developments in Europe are gaining pace and we are also focused on the Latin America region where developments in Mexico are anticipated and working groups in Brazil have now been established. We are well positioned to influence regulators and the industry through chairing the Association of Global Custodians T+1 Working Group in the U.S. and co-chairing the Association of Financial Markets in Europe (AFME) T+1 efforts and being a member of the U.K. HMT Accelerated Settlement Taskforce.

Equally, CSDR in the EU has required targeted and sustained advocacy to limit potential cost and risk to our clients which led to the deferral of the mandatory buy-in regime and more recently culminated in the CSDR ReFIT striking the right balance between incentivisation and penalisation. The focus for the global securities industry now is to make improvements to settlement efficiency and to remove the friction out of post trade processes, as such, we are focused on the efficiency and automation of post trade processes through our partnerships and investments in FinTech's such as Access Fintech and with FMI partners such as DTCC and SWIFT.

Asset Servicing and Tax both continue to be areas which require ongoing industry engagement and advocacy to improve regulatory proposals, market standards and efficiency; for example the Shareholders Rights Directive II which is currently subject to a review

and Withholding Tax reform in Europe, as well as in the proxy voting, events handling and income claims space, for example, in Mexico, where we are advocating for hybrid and electronic voting. We are also continuing to advance our use of alternative providers and improved processing for proxy voting.

Meanwhile, **Financial Market Infrastructures** have continued to focus on their operating models to ensure they are delivering value and efficiencies for the industry (e.g., DTCC Match 2 Instruct) and innovating (e.g. SWIFT UTI initiative), improving resilience (e.g., the work done with Euroclear U.K.&I) and reducing their costs - which all require engagement and dialogue from our business. At the same time, we are actively engaging in industry discussions on reviewing current market post-trade infrastructures to make them more competitive and resilient.

Digital Crypto Assets have been another key focus area for regulators, policymakers and our clients with the publication of Bank of International Settlements (BIS) rules on capital, the Securities & Exchange Commission (SEC)'s publication of its Staff Accounting Bulletin (SAB) AB 121 guidance, and finalisation of legislation in the EU such as Markets in Crypto Assets Act (MiCA) and the DLT Pilot Regime for Financial Market Infrastructures. The focus from industry and regulators continues, particularly given regulatory concerns regarding protection of clients investments and funds, and potential contagion risk into the traditional financial sector.

Meanwhile, 2023 has so far been a busy year with multiple regional and local regulatory consultations and market developments including the U.K. which, post BREXIT, is evaluating and introducing regulatory reforms intended to balance growth, competitiveness and innovation whilst the European Union (EU) is pursuing financial sovereignty objectives alongside innovation, payments and reviews of post-financial crisis regulation. However, the recent HM Treasury and European Commission U.K.-EU Memorandum of Understanding (MoU) agreed in May, represents a positive sign of dialogue between the EU and the U.K. which may bring more coherence and promote standardisation in future financial regulations whilst preserving financial stability, market integrity, and the protection of investors.

Please note this document was drafted in August 2023 and developments may have evolved since its drafting and subsequent publication in September 2023.



Settlement Acceleration

Settlement cycle acceleration is a growing global priority which impacts all actors in the trade to post trade value chain including Investors, Custodians, Broker Dealers, and Central Securities Depositories (CSDs). With India's T+1 implementation now complete and the United States and Canada confirmed for May 2024 we expect policymakers and financial market infrastructures to continue to focus on this for years to come.

J.P. Morgan Custody continues to advocate for an orderly and efficient post trade environment, and whilst accelerated settlement is a natural progression to reduce the risk between trade and settlement it does need to be evaluated on a market by market basis due to different nuances, market structure and legal/regulatory obligations, as such, our advocacy has and will continue to take a market by market approach.

Americas

U.S. T+1

On February 15th, 2023, the SEC published its Shortening the Settlement Cycle Final Rule, which will amend the standard settlement cycle for Depository Trust Company (DTC) eligible trades to T+1 with a compliance date of May 28th, 2024. The instruments subject to T+1 include equity, corporate bonds, municipal bonds, unit investment trusts as well as exchange traded funds (ETFs), American Depositary Receipts (ADRs), rights, and warrants settling at DTC. This is seen by many as a huge development in international securities markets and will remove the T+2 status quo which has been the default for many markets since the U.S. moved to T+2 in 2017.

Our firm has, and continues to be actively engaged in the U.S. T+1 industry and regulatory discussions and, for example, provided input into multiple industry comment letters (including letters from the Securities Industry and Financial Markets Association (SIFMA), Investment Company Institute (ICI), and Association of Global Custodians (AGC) which informed the SEC's final rules).

J.P. Morgan Custody is the Chair of the AGC T+1 Working Group which drives the custody industry's engagement in T+1 and is also an active member of the T+1 Industry Steering Committee and associated working groups, coordinated by SIFMA, the ICI and DTC, which continue to support the industry's implementation of T+1 in the lead up to May 28th, 2024 and will continue to bring any issues identified to the fore.

We continue to raise awareness for clients and the wider industry through participation in industry panels and webinars, such as the Depository Trust & Clearing Corporation's (DTCC) T+1 webinars, as well as through J.P. Morgan publications such as our T+1 FAQ document, our 2022 client article and audio recording on T+1 and through client events such as our recent T+1 Client Roadshow.



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Canada T+1

Due to the number of securities that can be listed in both Canada and the U.S., it was recognized that investors would benefit if both markets adopted the T+1 cycle at the same time, as such Canada will move to a T+1 settlement cycle on May 27th, 2024.

Our firm, amongst other industry actors and trade associations such as SIFMA and the AGC, advocated for both Canada and the U.S. to move to T+1 in lockstep on September 3rd, 2024 which is a public holiday weekend for both markets. However, due to the U.S. committing to May 28th, 2024, which is a public holiday in the U.S. but not in Canada, the Canadian move to T+1 will now take place one day earlier than the U.S. on May 27th, 2024.

J.P. Morgan Custody has engaged with our Canadian sub-custodians and the Canadian Capital Markets Association (CCMA) on T+1, and we support the Canadian market agreeing a transition date as close as possible to the U.S. T+1 transition. Although the date has been set for May 27th, 2024 the industry is waiting for the Canadian Securities Administrators (CSA) to publish its final rules which will determine other aspects such as the matching deadline in Canada which we understand from a recent CSA Staff Notice (August 10th, 2023) has been recommended to be 03.59am T+1 Eastern Time rather than the Trade Date 9pm deadline that was recommended in the 2022 Proposed Amendments to the settlement cycle. It remains a watching brief what the Canadian decision makers will recommend and we will notify clients by Newsflash as soon possible.

Mexico T+1

Although at the time of drafting this document there has not yet been a formal announcement from the Mexican regulators confirming the move to a T+1 settlement cycle, based on discussions with our sub-custodian and with local market infrastructure and brokers, we expect Mexico to move to T+1 settlement on the same date as Canada on May 27th, 2024.

J.P. Morgan Custody is advocating for Mexican regulators to make a formal announcement as soon as possible. Indeed, we understand that the Mexican Association of Stock Brokers (AMIB) submitted a formal letter to S.D. Indeval, the Mexican CSD, and Contraparte Central de Valores de México, S.A (CCV), the Mexican CCP requesting an official statement be published.

Anticipating an announcement confirming the Mexican markets move to T+1, market participants have already begun collaborating to analyse the impact on current operational processes, technology requirements and identify any obstacles to T+1 implementation.

At this time we do not expect any other LatAm markets to transition to T+1 at the same time as the U.S., Canada and Mexico however it remains a watching brief. Our current understanding is that:

- **Colombia, Peru, Chile:** T+1 is not currently a priority due to existing market implementation commitments meaning that it is currently unlikely that T+1 will be implemented in 2024
- **Brazil:** While B3, the Brazilian CSD, has started to hold initial meetings with local brokers and custodians to discuss shortening the equities settlement cycle to T+1 and to identify gaps and possible risks, it is unlikely that a move will occur in 2024
- **Argentina, Costa Rica, Panama:** There is no current indication that T+1 is being considered and it is therefore unlikely that there would be an implementation in 2024

Asia Pacific

Australia T+1

The Australian CSD, ASX, recently surveyed its participants for their opinions on shortening the settlement cycle for equities from T+2 to T+1.

We welcomed the survey and solicitation of industry views and provided feedback to ASX recommending that detailed analysis be conducted on all settlement flows in addition to evaluating the implementation/post-implementation experiences of other T+1 market migrations before committing to any changes or proposing a transition date. With the market already focused on the CHES Replacement System implementation, J.P. Morgan Custody considers that a move to T+1 would need to be considered in and around this programme, which could also impact an implementation timeline.

Philippines T+2

While T+1 appears to be a topic of increasing interest in certain markets/regions, the Philippines only recently moved to T+2 (from T+3) on 24th August 2023 reinforcing that there yet to be global alignment of securities market's settlement cycle conventions.

In May 2023 the Securities Clearing Corporation of the Philippines verbally informed market participants of their intention to amend the settlement cycle from T+3 to T+2 to become effective from June 9th, 2023. This provided little over one month for investors to be ready for such an impactful change.

Through its sub-custodian, J.P. Morgan Custody advocated for an extension to the implementation date in order to provide market participants adequate time to assess the impact of the shortened settlement cycle and to make any processing changes.

The migration date was subsequently moved to August 24th, 2023.

Europe

U.K.

An Accelerated Settlement Taskforce was introduced by the U.K. Government in December 2022 through His Majesty's Treasury (HMT's) Edinburgh Reforms.



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The Taskforce has been given the mandate by HMT to explore the opportunity for U.K. securities to move from a T+2 settlement cycle and, if the analysis supports, to consider how a shortened cycle could be implemented.

The Taskforce will produce an interim report for the U.K. Government by the end of 2023 and a full report with recommendations by December 2024 that will weigh-up the benefits, costs and risks for both U.K. and overseas investors, market participants and issuers, assess the challenges proposing solutions where possible including opportunities to leverage solutions deployed by other jurisdictions. The report will also consider FX, time-zone differences, different transaction types and asset classes.

We are a member of the Taskforce and currently co-lead the Operational Deadlines and Corporate Actions workstreams.

European Union

Through the CSDR ReFIT (see next section) the European Securities & Markets Authority (ESMA) have been mandated to assess the feasibility of shortening the settlement cycle in the Union and submit a report of findings to the European Council and European Parliament one year after the entry into force of the ReFIT regulation which we estimate will be in Q4 2024.

The mandate, which is similar to the U.K. Government's, requires ESMA to assess the costs and benefits of such a move differentiating between different transaction types and financial instruments, include an overview of international developments and any impact they may have on the region's capital markets and to outline how a move to a shortened settlement cycle could occur.

To front-run any future developments, including international developments, the region's trade associations have united to form a new Industry Taskforce to assess the feasibility of a T+1 settlement cycle in the Union and will form an opinion through taking a trade lifecycle approach including targeted evaluation of certain asset classes and transaction types. J.P. Morgan Custody, as co-chair of AFME's Transaction Clearing and Settlement Committee who have been looking at T+1 is a member of this new EU T+1 Task Force.

Middle East and Africa

Nigeria

In July 2022, the Nigerian Depository (CSCS) indicated that it intends to move from T+3 to T+1 after having initially stated that the cycle would be reduced to T+2, however, we understand that no formal publication of a date or any amendments to market rules have been made by CSCS at this time.

Due to the need for market infrastructure to be enhanced before T+1 can be considered, J.P. Morgan Custody has been advocating via the AGC and its sub-custodian for a programme of work to improve market automation.

The AGC requested an opportunity for a workshop with CSCS to discuss the market infrastructure enhancements required prior to implementing any amendment to the settlement cycle. The necessary enhancements include:

- CSCS plans to move from a dual account to a single account structure would need to be implemented prior to a reduction in settlement cycle
- Clarity of how Certificates of Capital Importations (CCIs) would be supported in a T+1 settlement cycle
- Weekly RTGS system outages would need to be resolved prior to a move to T+1
- Current non-STP market settlement processes would need to be addressed

We understand that CSCS is reviewing feedback and facilitating a working group, in conjunction with the AACN (Association of Asset Custodians of Nigeria) to work through all the above points.

Qatar

The Qatar Central Securities Depository (QCSD) and Qatar Stock Exchange (QSE) are planning to shorten the settlement cycle from T+3 to T+2 to be effective in January 2024 (date tbc). The first round of testing has taken place but results are yet to be announced. J.P. Morgan Custody are monitoring developments and will notify clients of any updates via Newsflash.



Settlement Efficiency

Settlement efficiency is at the heart of the securities post trade industry, impacting all actors from the investor through to the CSD. It is a priority topic for all divisions of J.P. Morgan's Corporate and Investment Bank including Custody.

While settlement efficiency has been assimilated with the CSDR 'Settlement Discipline Regime' in Europe, which we cover below, it is now increasingly seen as an enabler for T+1 making it much more of a 'global theme'.

Europe

The Central Securities Depository Regulation (CSDR) is a diverse regulation providing a common regulatory framework for CSDs, however the rules around settlement efficiency and the settlement discipline regime have attracted the most attention. A key point of focus has been the mandatory buy-in regime (MBI), deferred in December 2021 until November 2nd, 2025.

CSDR ReFIT

On June 27th, 2023 political agreement between the European Council and European Parliament was reached concluding the review of CSDR which first commenced in October 2020. Settlement discipline measures were again a key focus area and were subject to certain amendments including:

Mandatory Buy-In (MBI)

- The MBI will be retained in the CSDR ReFIT agreement and may be triggered by the European Commission (EC) to certain financial instruments or categories of transactions where the rate of settlement fails is not improving and is presenting a threat to financial stability. This is subject to a number of preconditions including consultation with the European Systemic Risk Board (ESRB) and based on a cost-benefit analysis provided by ESMA
- Before adopting the MBI, the EC is required to assess the effectiveness and proportionality of the penalty mechanism and, where appropriate, change its structure to increase settlement efficiency. It should also assess the cost implications of subjecting specific financial instruments and categories of transactions to MBIs
- Securities Financing Transactions (SFT) will be exempt from the MBI in addition to other exemptions that include “operations not considered trading” and settlement fails “not attributable to participants”. Exemptions will be specified by ESMA via Regulatory Technical Standards (RTS)

Cash penalties

- Certain exemptions have been agreed including “operations not considered trading” and settlement fails “not attributable to participants” which will be clarified by ESMA via RTS

Timing: Publication in the Official Journal of the final CSDR Refit is expected by the end of 2023. We anticipate that ESMA will commence work on the respective RTS’ later this year and throughout 2024.

J.P. Morgan have played an instrumental role in MBI related advocacy and have, for many years, advocated against the introduction of an automatic mandatory buy-in regime. It would have placed a disproportionate and negative cost and administrative burden on Custody clients whilst negatively impacting market liquidity which would in turn have increased costs to investors wishing to transact in the regions securities markets. We will continue to engage in this file throughout the RTS process and will keep clients apprised of developments.

J.P. Morgan Custody published a client audio recording on CSDR ReFIT in October 2022.



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Settlement Efficiency

With the MBI retained in the CSDR ReFIT, it is a priority to identify and understand the headwinds and limitations that challenge settlement efficiency throughout the securities trade to post trade industry throughout Europe.

Across the Corporate and Investment Bank, J.P. Morgan is closely engaged in different working groups advocating for the removal of structural barriers in the regions securities markets, and for cooperation and partnerships across sectors. Leadership roles in this area include:

- J.P. Morgan Custody: Co-Chair AFME Settlement Efficiency Taskforce: AFME will publish a study on the root causes of settlement fails in Autumn 2023 which will include a series of recommendations to optimise matching and settlement
- J.P. Morgan Custody: Co-Chair ECB Securities Group (SEG): The ECB SEG will focus on progressing the harmonisation and integration agenda across and beyond the T2S zone

- J.P. Morgan Prime Services: Co-Chair ICMA European Repo & Collateral Council (ERCC) which is focused on settlement efficiency to optimise market liquidity
- J.P. Morgan Prime Services: Member of the Euroclear Bank Settlement Efficiency Working Group

Our firm is also advocating for high quality, granular publicly available data based on a single methodology that should be used consistently by the regions CSDs, T2S, market participants, and vendors. There is presently inconsistency and divergence borne from different methodologies and scope across the industry which creates a distorted view of the current settlement efficiency rate and limits the identification of problem areas.

Financial Market Infrastructure Settlement Efficiency Initiatives

SWIFT Unique Transaction Identifier (UTI) Initiative

SWIFT’s UTI initiative aims to create a common reference for securities settlement transactions to be utilised across the post trade lifecycle by all parties. The rationale is to increase transparency and to create a common view of the matching and settlement status between the buyer and seller and any intermediaries they may use. This will promote the early detection of mis-matches through the settlement chain, avoid cross-matching and help to provide real time settlement statuses.

J.P. Morgan Custody participated in SWIFTs initial UTI pilot and believe that the UTI could help the industry with settlement efficiency, particularly as a number of markets move to T+1 over the coming years. Benefits come through wide industry adoption including across multiple markets and by integrating it into vendor solutions for post trade processing.

DTCC Match 2 Instruct

DTCC has enhanced its Central Trade Matching (CTM) product adding a new workflow called Match to Instruct (M2i).



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CTM - MATCH TO INSTRUCT WORKFLOW

This new feature further automates the post trade process, permitting the client to automatically affirm a trade, match, agree and settle the trade through the CTM platform. The process can be carried out throughout the trading day allowing the client to achieve same-day affirmation. Affirming a trade confirmation via M2i enables our clients to utilise our Direct Affirmation model, whereby J.P. Morgan Custody releases the CTM-affirmed trade to DTC after the customary checks are performed on the clients’ accounts meaning clients no longer need to send settlement instructions to us for M2i affirmed trades.

We consider this to be a positive evolution of post trade processing reducing the hand-offs and latency that will become time sensitive in a T+1 environment.

For more information on how M2i will be supported for U.S. T+1 please refer to our FAQ.



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Hong Kong - Launch of Northbound Bond Connect Online ‘One-stop Settlement Failure Reporting Service’

The China Foreign Exchange Trade System (CFETS), China Central Depository & Clearing (CCDC), Shanghai Clearing House (SHCH) and Bond Connect Company Limited (BCCL) jointly announced the launch of Northbound Bond Connect Online One-stop Settlement Failure Reporting Service which enables Northbound Bond Connect investors to review and confirm the online settlement failure reporting initiated by the onshore dealer. The product went live on June, 30th 2023.

We engaged with BCCL when they were designing the service suggesting that the new reporting service should streamline the entire reporting process for both onshore and offshore parties by removing the requirement for investors to physically sign the form, and to prevent duplicate effort for investors to submit the form to both BCCL and the Hong Kong Monetary Authority Central Money Market Unit (CMU) through the chain of Custodians.



Asset Servicing

The global trend to identify and address inefficiencies in the Income and Corporate Action processes continues. This is a priority topic for J.P. Morgan Custody who are active in the industry globally and hold a number of leadership positions.

Americas

U.S. LIBOR Transition

In December 2022, the Federal Reserve Board adopted a final rule to implement the Adjustable Interest Rate (LIBOR) Act. The Act identifies benchmark rates based on SOFR (Secured Overnight Financing Rate) replacing the London Interbank Offered Rate (LIBOR) for certain financial contracts after June 30th, 2023. In the U.S. this change impacts circa 100-150,000 securities and, due to the scale, updates are expected over a 6-month period.

To help ensure a successful transition, we engaged with the Alternative Reference Rates Committee (ARRC), a group of private market participants convened by the Federal Reserve Board and New York Fed, and actively participated in the AGC Asset Servicing Working Group to forge a consistent approach by the custodian community which ultimately agreed that reference data changes should not be announced as a corporate action thereby avoiding free format notifications which could have interfered with independent reference data sources.

U.S. Event Handling / Announcements

J.P. Morgan Custody is advocating for a ‘Golden Copy’ of Corporate Action Announcements which will significantly reduce the risk associated with Corporate Action events and deliver downstream processing and service efficiencies to our clients. This is essential for the buy-side community who may use more than one custodian and might therefore be exposed to divergent communication standards.

To achieve this, we are working with multiple groups including SIFMA, AGC, and DTCC to establish event announcement market standards and supporting the drafting of a whitepaper by SIFMA on how to improve event handling standards.

We are starting to see innovation in this space, for example, we participated in a pilot sponsored by SWIFT and Symbiont to establish whether DLT could be leveraged to address inconsistencies with corporate action announcements, and whilst the pilot was not able to progress (Symbiont filed for bankruptcy) we were supportive of its intent to create an accurate and consistent golden copy. Meanwhile, we are closely monitoring a DTCC partnership with Broadridge which intends to generate a golden copy.

Mexican Proxy Voting

Prompted by the COVID restrictions, J.P. Morgan Custody advocated through the AGC for hybrid and remote electronic voting. This was approved in April 2022 by the Chamber of Deputies but is still required to pass through the Senate for full approval. This final approval will provide issuers with the option to change their bylaws to allow remote voting and hybrid participation at the meetings. However, there is no regulation to dictate a standard for this process which could result in process fragmentation.

The next steps will be for the Stock Exchange and the Issuer community to pursue market standardisation including:

- Implementation of a Proxy Card
- Remote voting capabilities
- Standard requirements and deadlines for participation
- Standard presentation of results and confirmation of votes

Discussions continue and we understand that the Senate should provide its approval by September 2023 however it remains a watching brief.

Brazil Proxy Voting

The Securities and Exchange Commission of Brazil, Comissão de Valores Mobiliários (CVM) is reviewing regulations related to remote proxy voting which were first introduced in 2017. This review follows advocacy by our firm, in partnership with B3 (the Brazilian CSD) and ANBIMA (local trade association), which has focused on a number of areas including:

- Making it mandatory for companies to offer hybrid voting for Extraordinary General Meetings (EGMs) without members election and removing associated Power Of Attorney (PoA) requirements
- Improved reporting, for example, requiring B3 to confirm to custodians that remote voting instructions have been effectively delivered in meetings, and reporting the results of meetings
- Establishing the record date within remote voting rules – which would also enable improved reporting from J.P. Morgan Custody to its clients

If implemented, these changes will improve transparency and efficiency in the proxy voting process, and ultimately improve shareholder engagement opportunities for clients.

We now await feedback from CVM who we understand, following market feedback, are conducting some internal analysis and will issue a public hearing before releasing the new regulation.

Asia Pacific

Australia – Public Beneficial Ownership Register

The Australian Government has provided funding to establish a public register of beneficial ownership (BO) to record who ultimately owns, controls, and receives benefits from a company or legal vehicle (including trusts) operating in Australia. Entities in scope will be required to identify key Beneficial Owners (BO) i.e. those with an ownership interest exceeding 20 percent throughout the ownership chain. Certain BO information will be publicly disclosed.

J.P. Morgan Custody worked with the Australian Custodial Services Association (ACSA) to provide a response to the Treasury in respect of a Consultation Paper issued to solicit feedback on this proposal. The ACSA response conveyed our concerns and potential challenges to collecting and disclosing BO information.

Australia – Proxy Voting Modernisation

We are leading a custodian, vendor and client instigated initiative to advocate for a modernisation of the legislation and operating framework with regards to proxy voting in Australia, advocating for improved transparency, efficiency, and automation.

An industry whitepaper is currently being drafted which will recommend four key changes:

- Record date for voting to be set at the end of the business day
- Voting deadline to be set after record date
- Mandatory dissemination of proxy voting materials in electronic machine-readable formats
- Mandatory processing and confirmation of electronic proxy votes

Further industry and government advocacy efforts will take place following the publication of the white paper which is expected in Q4 2023.

Thailand – Corporate Action Announcement

J.P. Morgan Custody is working with its sub-custodian to advocate for improvements to the announcement of country related restrictions for voluntary events which are currently only announced after record date in a non-standardised format.

We are advocating for announcements to be made prior to record date with standardised announcement information. Combined, these improvements will increase transparency for Custody clients with regards to their eligibility to participate in the offer and increase straight through processing (STP) reducing the risk of client's instructions being rejected by the CSD. The AGC has submitted this position to the Stock Exchange of Thailand.

Europe

Shareholder Rights Directive (SRDII) Review

In Q4 2022 our firm provided feedback to an ESMA public consultation via AFME / AGC and the EBF, advocating for a regulation with a single pan-European definition of shareholder and a mandate to ensure there is a golden record for both corporate actions and general meetings.

At the end of July 2023, ESMA and the EBA published their findings in their Report on the Implementation and Effectiveness of SRDII with regards to the Proxy Advisors and Investment Chain provisions of the directive.

We are encouraged to see the extent that the ESMA and EBA recommendations reflect our own advocacy position in particular in respect of the following which will improve the exercise of our client's rights:

- Consider using a Regulation to harmonise shareholder identification, information transmission, and exercise of shareholder rights
- Consider introducing a standardised EU-wide definition of shareholder including beneficial owners OR provide issuers with the right to identify beneficial owners in addition to nominee shareholders
- Consider publishing a list of eligible securities
- Consider enhancing charging transparency by devising harmonised terminology for the types of charges and services which can be disclosed in a harmonised format
- Address uncertainties caused by varying applications of SRDII requirements across member states
- Harmonise the documentation required for shareholders to exercise their rights for general meetings, for example, recognising the confirmation of entitlement as the EU standard to allow shareholder participation in GMs
- Consider conducting an analysis of national rules and practices identifying harmonisation opportunities
- Consider extending the timeframe for shareholders to analyse and exercise their rights following the publication of meeting materials

Our firm has long advocated for these changes, including the need to simplify general meetings standards and bring them into line with corporate actions, and will continue to engage with EU regulators, issuer agents and other stakeholders in the run up to the European Commission's recommendations which we might expect in 2024.

European Central Bank (ECB) Single Collateral Management Rulebook for Europe (SCORE) Standards

The ECB AMI-SeCo (Advisory Group on Market Infrastructures for Securities and Collateral) have developed a set of standards and requirements to remove the barriers for the efficient movement of

collateral. Corporate Actions, Billing and Triparty were cited as areas for improved harmonisation. The deadline for compliance is March 2024 and the requirements apply to the regions CSDs, Central Banks, Triparty Agents and Custodians who interface with T2S / ECMS, although the ECB encourages compliance further down the custody value chain.

J.P. Morgan Custody has conducted an analysis of the SCORE Standards, identifying the standards relevant to custodians and submitted a survey to our CSD and agent bank network in order to identify any dependencies we may have on them. Meanwhile, we have a development programme in flight to be able to adhere to the standards (note the ISO 20022 capability requirement for custodians is due in November 2025).

Whilst there are no obligations imposed on our clients at this time we recognise that this will be of interest and will publish further information later this year regarding a potential expansion of ISO 20022 messaging to investor clients.

Middle East and Africa

Kuwait E-voting

E-voting was introduced in Kuwait as an interim solution during the COVID pandemic as physical voting at Annual General Meetings (AGMs) was limited by the COVID restrictions and was eventually made mandatory for issuers listed on the premier market. However, the mandatory implementation does not apply to those issuers listed on the main market which represents approximately 80 percent of the overall listings in Kuwait creating a split process for investors to follow.

J.P. Morgan Custody has advocated, via our sub-custodian and directly with the CSD, for e-voting to be mandated for issuers listed on the main market, which is expected to be implemented in 2023. We will keep our clients apprised of developments.



Tax

An evolving regulatory agenda coupled with a continuous drive across the industry for efficiency, digitisation and standardisation means that Tax is a dynamic area which we expect to continue for many years to come.

Americas

U.S. Internal Revenue Service (IRS) Certificates of residence

In a joint meeting between the Internal Revenue Service (IRS) and the Association of Global Custodians (AGC), held on March 30th, 2023, the IRS informed the AGC that they will modernise the burdensome and paper heavy 8802 Certificates of Residency process which has been much advocated for.

In a follow up meeting between the AGC and the IRS, held on July 13th, 2023, the IRS asked for feedback and advice on global best practices. Based on this meeting, the AGC is drafting a letter to the IRS outlining industry focused solutions including bulk upload requests and further automation recommendations in addition to suggestions on how to reduce naming convention issues.

Additionally, the IRS has made tangible progress to introduce J.P. Morgan Custody's request to issue rejection letters using a standard TIN format that allows our digital scanning processing to divert rejection letters to the correct accounts without manual intervention. This should accelerate and improve J.P. Morgan Custody's straight through processing.

Treaty exemptions on Canadian source dividends

Although DTC offers a tax service on Canadian securities, due to historical processes and the set up with the Canada Revenue Agency (CRA), not all entities eligible for treaty based tax exemption are able to secure the exemption for securities held at DTC.

Based on ongoing advocacy since 2019, including an AGC letter which we contributed to, DTC has informed the AGC that as of June 2023, they will offer U.K. and Swiss pensions the ability to secure treaty exemptions on Canadian source dividends paid through DTC.

Asia Pacific

Japan – Tax Relief for U.S. 81-100 Group Trust

U.S. 81-100 Group Trusts currently require onerous tax documentation which poses a significant obstacle for eligible investors to benefit from the U.S.-Japan double tax treaty. Although some Japanese Tax Offices accept simplified documentation, this is not a consistent market-wide practice.

To improve the process, J.P. Morgan Custody has engaged in discussions with the Japanese authorities, including the Japanese Financial Services Agency (FSA), to raise concerns and has proposed a unified and simplified documentation requirement. J.P. Morgan Custody will continue to monitor developments and engage with the FSA where required.

Korea – Process for Korean Treasury Bond (KTB) and Monetary Stabilisation Bond (MSB) exemptions

The Korean National Tax Service (NTS) has published new forms to support the Korean Treasury Bond and Monetary Stabilisation Bond tax exemption process for non-resident investors which imposes administrative hurdles for fund-type investors to benefit from tax relief.

We are working with the Asia Securities Industry & Financial Market (ASIFMA) Operational and Transactional Taxes Subcommittee to draft a comment letter to express industry concerns and propose solutions to the NTS.

Thailand – Financial Transaction Tax (FTT)

Draft legislation has been proposed which, if passed into law, would impose a new transaction tax on Thai equity trades. J.P. Morgan Custody has worked with ASIFMA to advocate with the Thai regulators to withdraw the draft legislation due to the impact on the Thai securities markets.

Further to the ASIFMA paper submission, the Thai Government has put the FTT proposals on hold. Our firm expects to continue its advocacy efforts depending on the position of the newly elected Thai Government.

Europe

EU withholding tax harmonisation 'FASTER'

On June 19th, 2023, the European Commission (EC) released its proposal for a Council directive on the 'Faster and Safer Relief of Excess Withholding Taxes'. The directive aims to promote fairer taxation, fight tax fraud and support cross-border investment throughout the EU.

Since the launch of the Capital Markets Union Action plan in 2020 and leading up to the proposed directive, including a public consultation in April 2022, the EC has periodically met with industry stakeholder groups to discuss their plans and proposals for streamlining withholding tax procedures across Member States to support cross-border investment and fight tax fraud. J.P. Morgan Custody participated in these meetings through the Association of Global Custodians (AGC) and U.K. Finance International Custody Tax Working Group (ICTWG), and advocated for the introduction of common electronic procedures, emphasising the importance of standardisation and clarification of processes including reporting, and the availability of any new procedures to both non-EU resident and EU resident investors alike.

The proposal includes the following measures:

- Adaptation of common EU electronic certificates of tax residence

- Implementation of a Certified Financial Intermediary (CFI) regime. CFIs will be able to process Relief at Source and/or Quick Refund procedures to complement any existing standard refund procedures
- The CFIs to have standardised reporting obligations to the income source member state Tax Administrations, including information on the tax relief received, beneficial owner as well as any financial arrangements that the CFI may be aware of that are linked to the underlying security

Stakeholder groups had until August 16th, 2023 to submit comments on the proposal. We provided feedback through the AGC and U.K. Finance ICTWG. The commentary will be summarised by the EC and presented to the European Parliament and Council during the legislative negotiations. The regime is expected to enter into force on January 1st, 2027.

Germany withholding tax modernisation bill

In June 2021 the German Parliament passed legislation to modernise procedures related to withholding taxes in the German market, including an electronic reclaim filing procedure (e-filing), removal of paper-based tax vouchers, and additional tax reporting obligations.

Post the introduction of the legislation, we provided feedback to the German Tax Authority (GTA) on the new e-filing portal (BOP) through the Association of Foreign Banks (VAB), U.K. Finance ICTWG and the AGC citing concerns with the BOP's inability to support mass reclaim uploads (single income payment and beneficiary information must be keyed in manually) and the related liability for custodians facilitating the e-filing of reclaims on behalf of clients.

The paper-based procedure ended on June 30th, 2023, subject to certain limited extensions for Swiss resident investors and claims facing statute at the end of 2023. Our firm is continuing its advocacy efforts to extend the use of the paper-based procedures until a mass upload functionality is made available and is also taking part in a GTA Working Group to develop bulk filing capabilities which commenced work in July 2023.

The German Withholding Tax Modernisation Bill also introduces changes to the issuance of tax vouchers to support reclaims which will route directly to the GTA provided all participants in the chain of custody provide the required information. The changes will be effective from January 1st, 2025. There is currently a lack of information available from the GTA but we continue to actively track and will advise clients of developments through J.P. Morgan newsflashes.

Austria change in the Tax Reclaim entitlement date

In November 2022, the Austrian Ministry of Finance released updated guidance clarifying that tax reclaim entitlements will be determined based on holdings as at Annual General Meeting (AGM) -1 (rather than ex-date -1). The updated guidance applies to past, open, and new reclaims. There has been no change to income entitlement processing.

J.P. Morgan Custody provided feedback directly to the Austrian Ministry of Finance (MOF) on the challenges imposed by the change, including the use of different entitlement criteria for tax and income, and challenges relating to the retrospective collection of undue tax relief based on the updated guidance.

On July 21st, 2023, the Austrian Government published the Austria Tax Amendment Act 2023 which aligns reclaim entitlements to the investor's end of dividend record date position and provides additional requirements for investor eligibility for withholding tax reclaims on Austrian sourced income. The additional requirements provide that the claimant bear appropriate economic risk and be the continuous economic owner of the underlying shares during a minimum holding period of 45 days, within 45 days before and 45 days after the dividend record date. The changes introduced are effective for dividend income payments with record dates after June 30th, 2023. Further guidance on the implementation is expected within the coming months. Our firm is working with the U.K. Finance ICTWG and directly with the MOF to provide feedback and obtain further clarity.



Financial Market Infrastructure Developments

Beyond tools to improve settlement efficiency, Financial Market Infrastructure providers continue to develop new products and build upon their strong market position within post trade. These developments require our ongoing engagement as they can impact our clients, cost and operating models, but also present opportunities.

Americas

Federal Reserve's Securities Services Automatic Claims Adjustment Process (ACAP)

ACAP is the Federal Reserve's Securities Services (FSS) initiative to support the tracking and payment of income to beneficial owners for repo, fails, and interim accounting for Agency Mortgaged Backed Securities (MBS).

J.P. Morgan Custody has been actively participating in industry discussions with SIFMA and the FSS via its Governance Council and Working Group to ensure the suggested approach is fit for purpose, is suitable for our clients, and to promote awareness and support across the wider industry, including the securities lending providers, broker dealers, and clients.

Phase 1: Implemented January 2023

- FSS has recently expanded this service by implementing intraday payment processing via Fedwire to Depository Institutions

Phase 2: TBC

- FSS plans to include two new security types (U.S. Treasury and Agency Debt Interest Bearing securities) and one new claim type (Securities Lending for FSS eligible security types) to Depository Institutions
- This phase was originally planned for an August 2023 implementation, however, it was agreed that it should be postponed to allow industry participants time to assess readiness and challenges with the current service offering

A Phase 2 replanning workshop session is scheduled for Q3 2023 to ascertain if the service will be either a) cancelled or b) rescheduled to 2025. Much will depend on whether the existing challenges have a path forward for industry adoption or not.

If Phase 2 does go ahead it will benefit our clients who will no longer have to manually claim for interest or coupons relating to fails or repo / loans as FSS will automatically debit / credit beneficial and actual holders on the payable date based on the record date position.

Asia Pacific**Australia - CHES replacement project**

The Australian CSD, ASX, is replacing its settlement and clearing system 'CHES' which has been in use since 1992.

Our firm has been involved with the project since its inception in 2015 advocating for standardisation, digitisation and automation within the market.

Following the release of an independent report by Accenture on the delivery of the CHES Replacement System, on November 18th, 2022, ASX announced that all development work on the distributed ledger-based system has been paused. In its mid-year results ASX provided an update on the next phase of the project, which include:

- Potential move away from using DLT
- A review of the world's top 20 exchanges clearing and settlement systems

- RFI underway to gather information from potential software vendors
- A 70 million AUD fund to support development costs
- A target of December 2023 to choose the vendor and system design
- New Technical Committee to be established to provide guidance and direction on the replanned design, testing and implementation

We continue to monitor and partner with ASX on this key initiative.

Hong Kong - HKD-RMB dual counter initiative

In September 2022, the China Securities Regulatory Commission (CSRC) announced an objective to further enhance Hong Kong's position as an offshore Renminbi (RMB) centre. Subsequently, HKEX introduced a new HKD-RMB dual counter model in the Hong Kong securities market to allow investors to trade, settle and interchange eligible dual counter securities in the RMB counter which went live on June 19th, 2023.

Leading up to the implementation, J.P. Morgan Custody was actively advocating with HKEX through bilateral meetings and via the Asia Securities Industry & Financial Markets Association (ASIFMA) to ensure that separate ISINs were assigned for the RMB counter. The successful advocacy resulted in all 24 eligible dual counter securities carrying a separate ISIN at the launch.

We have also advocated for HKEX to accept SWIFT instructions for inter-change transfers between counters instead of manual CCASS input, and that the Singapore model is adopted i.e. 2 counters for trading and 1 counter for clearing and settlement as a long term solution which will eliminate the need to perform interchange transfers in the market. J.P. Morgan Custody will continue to advocate for these changes and will continue to follow up with HKEX and participate in industry working groups to achieve long term solutions to improve market efficiency and scalability.

Philippines

Philippine market infrastructures, in particular the Equity Depository and Clearing Corporation, have faced multiple outages in the previous year. Currently, there is no formal contingency framework or protocol that the market should follow in the event of a system outage.

J.P. Morgan Custody has partnered with its sub-custodian and the national market practice group in the Philippines to advocate for the Equity Depository and Clearing Corporation to introduce a playbook that outlines the protocols that market participants should adopt in the event of an outage impacting market settlement. This will be beneficial for the entire market and will provide a quicker turnaround of market information and defined settlement protocols for all to follow in the event of an outage. The playbook is currently under review with the securities regulator.

Europe

CREST Modernisation Roadmap

J.P. Morgan Custody is engaged in ongoing collaboration with the U.K. CSD, Euroclear U.K. & International Limited (EUI) with regards to adequate transparency of its 8-year platform modernisation programme which is due to conclude in 2030. We are a key participant in all U.K. Senior working groups coordinated by the CSD, including EUI U.K. User Committee, Senior Client Advisory Group, and EUI Market Resiliency Group where it continues to shape and influence topics of importance to the U.K. market. Key topics of discussion with EUI have, of late, centred around platform stability and the associated steps taken to mitigate settlement suspension scenarios, product uplift roadmaps and timeline, as well as the potential move to T+1 settlement in the U.K.

As part of its multi-year platform modernisation initiative, our current ongoing dialogue with EUI is on the immediate 2-year roadmap of deliverables which include, amongst others, the following:

- Dividends in CREST (CRESTPAY): Continued advocacy with EUI for full adoption by all participants, specifically by issuers
- Platform Modernisation: Focus on technical improvements to reduce systemic risks around EUI's 'Important Business Services' and to enhance platform stability
- Access Modernisation: Including a new 'front end' to the CREST GUI (expected 2024) and ISO 20022 messaging adoption
- Asset Servicing Modernisation: Market engagement including the need to establish working groups in order to finalise a roadmap of deliverables from 2026 onwards (for example: migration sequencing, message mapping, co-existence of platforms for a period of time)

Meanwhile, extensive advocacy has successfully resulted in a new CREST GUI release in September 2023 which will enable clients to bulk upload transactions. This will be particularly beneficial in the event of a technology outage providing a viable contingency arrangement.

We will closely monitor the CREST Modernisation Roadmap and will provide updates in due course.

Middle East and Africa

Kingdom of Saudi Arabia Post Trade Technology Programme (PTTP) 2.0

Post the successful implementation of the CCP, NASDAQ Clearing System, and the NASDAQ CSD System in April 2022, the Saudi Stock Exchange / CSD has kick started the second phase of its post trade technology programme (PTTP), which is primarily designed to incorporate feedback / suggestions from all market participants on their experience over the past few months since implementation. To assist with this effort, J.P. Morgan Custody, as members of the PTTP-2.0 working group, has provided comprehensive feedback on the existing processes and systems that require improvement which include:

- The ability for the automation or bulk processing of proxy votes
- Further refinement of the cash compensation process and the ability to provide adequate client reporting
- Trade referencing alignment between the communication channels at Tadawul, Muqassa and Edaa which will help overcome some of the technical

and operational challenges currently faced across the market

- Extension to the trade management window on T+0, which currently closes at 16:00 hrs, to provide more flexibility for international clients to manage their trades
- Improvements to cash dividend distribution in the local market to bring uniformity and alignment with other events - the existing dual process i.e. some managed by the CSD Paying Agency team and some directly managed by the Issuers, creates operational challenges and risk
- Improved functionalities for negotiated deals

During PTTT Phase 1, our firm was heavily engaged in the market dialogue to standardise SWIFT message types within the new NASDAQ CSD system among many other nuances.

Bahrain – Implementation of DVP

Bahrain operates a dual account structure which requires local custodians to transfer securities from a client's custody account to the client's trading account, prior to the broker being able to instruct the trade on the exchange. Meanwhile the current local settlement process is conducted directly with the broker via the CSD, without a Delivery Versus Payment (DVP) model in place.

J.P. Morgan Custody has been directly advocating with the CSD and via our sub-custodian in Bahrain, alongside the Association of Global Custodians (AGC) for a DVP model that will minimise settlement exposure.

A draft DVP model has been published to the market and feedback has been collated. A final version will be circulated prior to the CSD announcing a go live date, which is expected to be announced during in 2023.



Digital / Crypto Assets

Digital / crypto assets (i.e., cryptocurrencies, tokenised and native digital securities, stablecoins, Central Bank Digital Currencies (CBDC), Non-Fungible Tokens (NFTs) etc.) continue to be a key area of focus for global regulators and policy makers who are keen to avoid spill-over effects of recent market events into the mainstream financial sector. We expect regulatory focus to continue and we remain closely involved in industry input on policy and regulatory initiatives, while collaborating on J.P. Morgan branded digital projects.

Global

Bank of International Settlements (BIS)'s Basel Committee for Banking Supervision (BCBS) Proposal on the prudential / capital treatment of crypto assets

The BIS / BCBS proposal can be seen as a key piece of crypto asset regulation providing a framework for the prudential risk management of digital / crypto assets which also includes tokenised securities, stable-coins and cryptocurrencies.

Our firm influenced industry letters from the Global Financial Markets Association (parent group for SIFMA/AFME/ASIFMA), AGC and American Bankers Association (ABA) advocating for the 'same activity, same risk, same treatment' to ensure that crypto-assets benefit from the same high standards of risk and a comprehensive prudential framework as 'traditional' assets do.

In December 2022 BCBS confirmed in its final recommendations that:

- Custody has been explicitly carved out from the credit, market and liquidity risk requirements for crypto-assets, while remaining subject to operational risk requirements.
- A proposed fixed add-on for infrastructure risk to establish a flexible approach that allows regulators and central banks to impose an add-on based on any observed weaknesses in the DLT infrastructure that underlies specific crypto-assets. Banks who can demonstrate that the infrastructure risk for these assets has been adequately addressed, could therefore avoid the infrastructure risk-add on and its associated costs.

IOSCO consultation on Policy Recommendations for Crypto and Digital Asset Markets

In May 2023 IOSCO launched a consultation seeking feedback on its policy recommendations for crypto and digital assets. This effort is part of IOSCO's Crypto-Asset Roadmap for 2022-2023 and is designed to improve global standards for the regulation of crypto-assets and outlines how investors should be protected and how crypto trading should meet the same high standards that apply in 'traditional' markets. The recommendations cover six key areas, which are consistent with the IOSCO Objectives and Principles for Securities Regulation and relevant supporting IOSCO standards, recommendations, and good practices:

- Conflicts of interest arising from vertical integration of activities and functions
- Market manipulation, insider trading and fraud
- Cross-border risks and regulatory cooperation
- Custody and investor asset protection
- Operational and technological risk
- Retail access, suitability, and distribution

We contributed to a number of industry association submissions including GFMA, AGC and FIA advocating for:

- A distinction between custody and other services (as they have been amalgamated into a single definition of a Crypto Asset Service Provider (CASP) which is not appropriate)
- Differentiating between retail and institutional investors (important for risk disclosures)
- Focus on potential conflicts of interests e.g. between trading and post trade
- Existing rules to be leveraged where possible

Americas

SEC staff accounting bulletin for crypto assets

In February 2022, the SEC issued guidance requiring filing firms to hold a liability and corresponding asset on their balance sheet to reflect the fair value of any "crypto assets" which are being safeguarded for their clients.

This stance goes against the traditional treatment of assets held in custody where securities are treated as the property of the client (not property of their custodian), and therefore not reflected as a liability for the custodian on its balance sheet.

The SEC's definition of "crypto assets" is very broad and arguably captures safekeeping of any type of asset on public and private DLT, therefore potentially capturing several current and future J.P. Morgan initiatives.

Our firm provided significant input into industry discussions and influenced formal industry letters to SEC, U.S. Treasury and U.S. Federal regulators. These letters outlined the current regulatory framework for banks with regards to traditional custody and protection of clients assets and how similar principles and rules should also apply to digital / crypto asset custody provided by banks.

Europe

EU Markets in Crypto Assets (MiCA)

MiCA is a new EU wide legislation which will regulate the crypto-asset markets and aim to provide investor protection and financial stability. The regime defines the categories of crypto assets primarily focussing on cryptocurrencies and stablecoins but not financial instruments which fall under the DLT Pilot Regime (see EU DLT pilot regime below).

After lengthy political negotiation and industry advocacy, the European Council and Parliament reached agreement on the final legislation which makes it the first major regional legislation on crypto assets. The regulation is expected to come into effect in December 30th, 2024.

MiCA requires crypto-asset service providers (CASPs) to seek authorisation in the EU before providing their services, and sets out rules covering issuance, disclosures, governance and capital requirements in addition to custodial liability for loss of assets caused by external events which all aim to achieve investor protection.

Our firm contributed to AGC and AFME advocacy efforts and will continue to monitor developments including anticipated public consultations which will help to shape the delegated regulation(s).

EU DLT pilot regime

The DLT pilot regime provides a pan-EU testing environment which allows financial market infrastructures (FMI) to apply to operate a DLT-based trading facility and/or settlement system for digital assets which qualify as financial instruments under MiFID (e.g., securities) within a flexible regulatory environment. The pilot commenced in March 2023 and will run for 6 years.

The regime is temporary and optional to develop a market infrastructure for digital securities and to help inform EU regulators as to what (if any) permanent changes to the regulatory framework would be beneficial.

While there are no direct requirements for J.P. Morgan Custody or our clients, we will monitor the progress of applicants in the pilot which may inform our DLT strategy / advocacy, and will feed into ESMA consultations, including on applicable law and governance arrangements.

U.K. FMI sandbox

HMT are leading an initiative to commence an FMI sandbox, to allow testing DLT technology in the production environment. The DSS (Digital Securities Sandbox) has been issued and is now open for feedback.

We are closely engaged in this initiative and actively contribute to industry and bilateral engagements with HMT.

The U.K. has also reviewed its property law for digital assets with final recommendations concluding that the current regulatory framework is largely in line with existing regulations. J.P. Morgan Custody was closely involved in the consultation and advocacy process through AGC, AFME and U.K. Finance.

Look out for: The evolution of the U.K.'s crypto asset regulation through the Financial Services & Markets Act 2023 (following HMT's public consultation that closed on April 30th, 2023) and continued dialogue from HMT and BoE on the case for a digital pound (following a public consultation that closed on June 30th, 2023).



Regional Market Developments and Regulatory Outlook

Outside of the themes that we have highlighted in this paper, local and regional regulators continue to develop regulatory frameworks, improve market standards and resiliency. The following are some highlights, however not an exhaustive list.

Americas

SEC investment adviser custody rule

In February 2023, the SEC proposed a new rule under the Investment Adviser Act of 1940 that addresses custody of client assets. The proposal amends the current “Custody Rule” and intends to help ensure that qualified custodians (QCs) provide certain standard custodial protections when maintaining an advisory client’s assets. Funds registered under the Investment Company Act of 1940 (“Funds”) are at present not within the scope of this proposal.

The proposal widens the scope of assets covered by the custody rule beyond funds (money) and securities to “other positions held in a client’s account”; and requires registered investment advisers to enter into written agreements with QCs.

The proposal also requires registered investment advisers to obtain certain assurances in writing from their QCs. These assurances would require QCs to exercise due care; indemnify the client against loss resulting from negligence; fulfil obligations regardless of sub-custodial arrangements; clearly identify client's assets, hold them in a custodial account, and segregate them from the QC's assets; and not subject client assets to liens unless authorised to do so in writing. The investment adviser would need to monitor QCs to ensure compliance with assurances. The proposal would also impose certain additional requirements on Foreign Financial Institutions (FFIs).

J.P. Morgan sent an own name letter in May 2023 to the SEC in response to the proposed rule and we also participated in drafting a number of trade association letters including those from SIFMA, ABA, BPI, AGC, ICI and AFME.

SEC cybersecurity proposal

In February 2022, the SEC proposed new cybersecurity rules for Investment Advisers and "Funds" focusing on policies and procedures, incident management and notifications, disclosures, and oversight of key third-parties.

In March 2023, the SEC re-opened the comment period in light of other SEC proposals on cyber risk.

Our firm fed into industry association letters (e.g., SIFMA, BPI,) sent to SEC with the aim to get greater clarity on whether custody services are captured in the proposed rules.

We are monitoring the progress of this file and will review the final rule.

SEC outsourcing proposal

In October 2022, the SEC published a proposed rule on outsourcing for Investment Advisers. The proposed rule is designed to ensure that advisers meet certain minimum requirements when outsourcing covered functions to service providers.

J.P. Morgan Custody contributed to industry letters submitted by SIFMA and the ABA which raise the point that it is unclear if custody is in or out of scope of the proposed outsourcing rules.

The SEC comment period closed on December 27th, 2022 and a final rule is possible in H1 2024.

Asia Pacific

Australia – Prudential Standard CPS 230 Operational Risk Management (CPS 230)

In July 2022, the Australian Prudential Regulation Authority (APRA) released a consultation to introduce a new cross-industry Prudential Standard CPS 230 Operational Risk Management (CPS 230) which will set out minimum standards for managing operational risk, including updated requirements for business continuity and service provider management.

We welcome this initiative and improved standards to strengthen operational resilience in the Australian market and is closely monitoring developments.

India – KYC related disclosures

J.P. Morgan Custody continues to help clients navigate a dynamic regulatory environment in India. As regulatory frameworks around KYC (Know Your Customer) and disclosure tightens, our focus has been to highlight the practical challenges faced by foreign investors to meet additional KYC requirements and ongoing compliance, and to work with the regulators to improve the operating environment. Examples of our advocacy in this area include:

- Advocating for the synchronisation and consistency of KYC rules for foreign investors across SEBI and RBI
- Advocating to ensure foreign investors have adequate time to review, access and provide the additional KYC information if required

India – Enhancing the market entry process and operational processes for foreign investors

J.P. Morgan Custody has been leading industry discussions to recommend improvements to streamline and reduce the time to complete foreign investor market registration and onboarding processes recommending multiple changes which include:

- Adoption of scanned copies as opposed to original documents (which is the current requirement to complete KYC and market registration)
- Adoption of digital signatures and SWIFT confirmations instead of wet ink signatures and attestation of the physical documents
- Simplification of the market entry application form including the rationalisation of information and supporting documents

In addition to the above, we are advocating for enhancements to market protocol to maximise foreign portfolio clients ability to access and invest in the Indian market. Our recommendations include:

- Free of cost transfer of securities from one FPI account to another FPI account for genuine restructuring of the fund in its home jurisdiction
- Streamlining the process for claiming Relief at Source (RAS)
- Distribution of monetary corporate action proceeds through depositories
- Permit early pay-in (EPI) for settlement of government debt trades vs. the requirement to pay margin

Hong Kong – Supervisory Policy Manual on Operational Risk Management

In March 2023, the Hong Kong Monetary Authority (HKMA) published its revised Supervisory Policy Manual module on Operational Risk Management and revised its module on Business Continuity Planning.

Our firm considers this to be a positive development and underlines HKMA's commitment to strong governance and risk management in a market which continues to evolve and innovate.

South Korea – Foreign investor FX accounts

During COVID, the South Korean regulator relaxed the notarisation requirement on certain account opening documents for IRC applications, some of which the custodian banks leveraged for their client due diligence (CDD)/ KYC account opening. While the regulator will not issue new IRCs from December 14th, 2023, eliminating the requirement to submit any documents to the regulator, this leaves potential inconsistencies in the list of documents that each bank may request from a foreign investor for account opening.

J.P. Morgan Custody, through regular conversations with other custodian banks, has been constantly emphasising that the regulator should guide the banks to adopt similar requirements for account opening especially given that the removal of the IRC requirement is intended to ease the market entry for foreign investors not complicate it.

Europe

Capital Requirements Directive VI (CRD VI)

In July 2023 the European Council and Parliament reached a political agreement on the EU banking package (CRR3/CRD6) to implement the finalised Basel III standards. The agreement largely adheres to the international Basel standards with some EU specific changes to the framework, most of which will apply only transitionally.

Of note, new provisions include a requirement for third country institutions to establish a branch to provide certain cross-border services into the EU unless the client approaches the third country institution itself which is permitted under reverse solicitation.

J.P. Morgan Custody were advocating for the safekeeping and administration of securities (and safe custody services – physical custody) to be removed from the scope of CRDVI which has been confirmed as an exempt activity alongside payment services in the final text. We are currently evaluating the final regulatory text.

Look out for

*The European Union recently commenced work on its **Payment Services Regulation**, following its Review of PSDII, and Open Finance which were both subjected to public consultations in 2022.*

*The **EU Digital Operational Resilience Act (DORA)** is due to enter into force on 17th January 2025 and will provide a harmonised regime for ICT and cybersecurity risk and will introduce regulatory oversight for critical third parties e.g. cloud providers.*

*Meanwhile, the European securities industry awaits the European Commission's report of findings following the 2021 **Settlement Finality Directive** and **Financial Collateral Directive** public consultations.*

U.K.

Look out for

*The **'Financial Services & Markets Act' (FSMA)**, which seeks to repeal retained EU law, and **'Edinburgh Reforms'** have already triggered numerous public consultations by HMT this year which have included the Short Selling Regulation and Payment Services Regulation. To date, core 'securities post trade' regulations and directives such as CSDR (note that the 'settlement discipline regime' (Articles 6-8 of the*

regulation) was not on-shored by the U.K. as it entered into force post its withdrawal from the EU however the broader regulation applies), Settlement Finality Directive (SFD) and SRDII, have not yet stepped into the spotlight – but could. Our firm is closely monitoring the FSMB and the evolving U.K. regulatory environment.

Middle East and Africa

Kingdom of Saudi Arabia – QFI entry requirements

Following much advocacy which included the submission of a J.P. Morgan authored position paper to the Capital Market Authority (CMA) and copied to the Market Custody Committee in late 2022, the QFI entry requirements in KSA have been significantly relaxed including the removal of the QFI Application Form and Assessment Agreement. This development essentially aligns the Kingdom of Saudi Arabia with international market best practice. The regulatory amendment, which took effect in May 2023, has provided the following key benefits to J.P. Morgan Custody clients.

- Lessens the documentation/ administrative burden benefitting foreign investors’ account opening teams
- Fosters better market entry turnaround time for clients wishing to invest in the Saudi market
- Implicitly removes the role of local participants, essentially custodians, to act as Assessing Authorised Persons (AAP) that were previously required to review and certify a foreign investors eligibility to enter the Saudi market – again reducing account opening times

Kingdom of Saudi Arabia – Omnibus accounts for global custodians

The Saudi Capital Markets Authority’s permission to allow ICSDs to open Omnibus Foreign Nominee Accounts (OFNAs) for clients investing in the Saudi Fixed Income market from May 6th, 2021 was a positive step towards promoting foreign investment in the Saudi Arabian local debt market. Since omnibus accounts provide ease of market access for foreign investors, J.P. Morgan Custody believes that further foreign investor access can be achieved, by permitting Global Custodians to offer OFNAs to their clients, in particular to non-resident investors. Such a development would further support the development of the local debt market and increase liquidity.

In addition, this will benefit CMA licensed Capital Markets Institutions (CMIs), such as J.P. Morgan Custody, to complement and develop their local custody service suite. With an OFNA structure, J.P. Morgan Custody can demonstrate its:

- Scale through single point of entry with option of omnibus or segregated accounts in line with market and client requirements
- Asset safety and protection
- Full range of supporting products including network, tax, proxy regulatory capabilities, intelligence to deliver industry expertise, liquidity and FX solutions to maximise cash efficiency

We continue to advocate for OFNAs for Global Custodians and will keep clients apprised of progress.

Qatar – Qatar Central Securities Depository new account opening platform

The Qatar Central Securities Depository (QCSD) is working on a new account opening platform which will be introduced in 2 phases.

- Phase 1: Expected in Q3 2023, will provide sub-custodians with the ability to upload hard copies of documents to the Depository system. J.P. Morgan Custody’s sub-custodian has completed the required testing. (Physical documents will still be required to be provided at this stage.)
- Phase 2: The QCSD intends to reduce the number of documents required for account opening and simplify legal requirements so that soft copies of finalised documentation can be submitted to sub-custodians. The timeframe is unclear at this stage.

In recent years, J.P. Morgan Custody has been actively engaged with the QCSD advocating for the automation and simplification of account opening both bilaterally and through its sub-custodian.

This development, when fully implemented, is expected to ease clients access to the Qatari market, remove the requirement to provide personal information / documents when opening accounts, and to reduce the cost of opening accounts in this market. J.P. Morgan Custody continues to monitor developments and will inform its clients of progress including timeframes once agreed.

For additional information, please contact your J.P. Morgan representative.

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