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FINANCIAL SERVICES AND MARKETS ACT 2000 (REGULATED ACTIVITIES AND MISCELLANEOUS PROVISIONS) (CRYPTOASSETS) ORDER 2025 (the "draft statutory instrument")

TRAVERS SMITH LLP TECHNICAL COMMENTS

23 May 2025

These technical comments are submitted to His Majesty's Treasury ("**HMT**") on behalf of Travers Smith LLP ("**Travers Smith**" or "**we**"). Travers Smith is a leading, full-service international law firm based in the UK which has a long history of acting for major financial services clients, financial market infrastructures and central banks (alongside a wide range of other clients). In recent years, we have worked closely with FMIs and digital assets firms, including exchanges and custodians, using or planning to use DLT-based or other next-generation technologies to provide their services. We have also spent considerable time analysing the legal and regulatory issues associated with the use of digital assets in payments, clearing and settlement, as well as the tokenisation of securities and other assets.

These comments refer directly to the legislation as amended by the draft statutory instrument. The terms "**FSMA**" and "**RAO**" refer respectively to the **Financial Services and Markets Act 2000** and to the **Financial Services and Markets Act 2000 (Regulated Activities) Order 2001**. We have included both current and proposed references to RAO and FSMA. References to "Articles" are references to Articles in the RAO.

1. TREATMENT OF STABLECOINS USED AS INSTRUMENTS OF PAYMENT

1.1 We note the statement in paragraph 1.4 of the Policy Note, to the effect that there has been a policy decision not to integrate stablecoins into the Payments Services Regulations 2017 (**PSRs**) at this stage, but that HMT is supportive of their use in payments.

1.2 However, we are concerned that this decision has then had unintended consequences for the approach taken to the drafting, flowing from the inclusion of qualifying stablecoin (**QS**) as a subset of qualifying cryptoasset (**QCA**).

1.3 Specifically, and most seriously, a merchant accepting stablecoin as a means of payment in the United Kingdom would be at risk, on the current drafting, of carrying on the regulated activity of "dealing" as principal in the stablecoin. This is because the definition of "buying" in Article 3(1) includes acquiring an asset for valuable consideration – producing the result that providing (for example) goods in exchange for stablecoin amounts to the merchant potentially "buying" the stablecoin and so falling within the regulatory perimeter. We also have concerns that there could be a parallel extension of

the dealing as agent activity to firms facilitating the acceptance of payments using stablecoin.

1.4 We do not believe this to be the policy intention. It would constitute a huge obstacle to the adoption of stablecoin as a means of payment.

1.5 We consider that this could be resolved in at least two ways.

1.6 First, via an amendment to Articles 9W and 9Y to exclude from the dealing activities the acquisition, use or disposal of a QS (or any other QCA in the nature of an asset-referenced stablecoin) as an instrument of payment. An alternative would be to modify the application of Article 68 to achieve a similar result (although, for example, a "customer" would need to include an individual for this purpose) and to ensure that the relevant exclusions to the Articles 9U and 9X "dealing" activities expressly cross-refer to (or set out) the suitably modified Article 68.

2. DEFINITION OF A QUALIFYING CRYPTOASSET

Transferability of a qualifying cryptoasset

2.1 Under Article 88F(1)(b), a QCA must be transferable. Article 88F(2) gives a non-exhaustive definition of the circumstances in which a cryptoasset is to be treated as transferable. Under Article 88F(2)(b), this includes where "*a communication made in relation to the cryptoasset describes it as being transferable or conferring transferable rights*". It is unclear what this provision is designed to achieve, and it risks causing material uncertainty about the intended scope of the cryptoassets regime.

2.2 One possibility is that Article 88F(2)(b) is designed to be a consumer protection measure so that a person who (for example) issues a non-transferable cryptoasset but falsely describes it as transferable would still be treated as carrying on the Article 9M issuing activity in relation to that cryptoasset. However, if that is the intention, we consider that the proposed drafting introduces a very significant level of uncertainty and may have unintended and undesirable consequences.

2.3 In particular, the proposed drafting raises the following issues:

2.3.1 Article 88F(2)(b) does not state *who* is making the relevant communication. Accordingly, applied literally, an unconnected third party issuing a communication that describes the relevant cryptoasset as transferable would result in the cryptoasset being treated as transferable for the purposes of Article 88F(1)(b) and, therefore, potentially constituting a qualifying cryptoasset – and this might be the case, even if the terms of issue for the QCA expressly and specifically prohibit or inhibit its transfer. This could have serious consequences for unrelated parties carrying out activities in relation to the cryptoasset on the understanding (which would be correct as a matter of fact, but rendered incorrect as a matter of law by virtue of Article 88F(2)(b)'s deeming effect) that the asset in question was not transferable and therefore was not a qualifying cryptoasset. For example, a person making

arrangements in connection with the asset in question might, by virtue of a statement made by an unconnected third party, unwittingly find themselves acting in breach of the general prohibition in s.19 FSMA (and therefore committing a criminal offence). That seems to be a highly unsatisfactory state of affairs, which we assume does not represent HMT's intention.

2.3.2 The nature of the communication in question is not qualified by reference to any particular knowledge or mental state. Therefore, an isolated entirely innocent but inaccurate description of a cryptoasset as being transferable seems to have the apparent effect of potentially rendering it as a QCA and activating the regulated activities regime.

2.4 If the intention behind Article 88F(2)(b) is to protect investors from being "mis-sold" a cryptoasset through false statements about transferability, we consider that it would be strongly preferable to address such risks through other frameworks, such as criminal liability (e.g. under the Fraud Act 2006 and/or false or misleading statements offences under the Financial Services Act 2012), the law of misrepresentation, or the fact that s.19 FSMA also applies to persons *purporting* to carry on a regulated activity, even if they are not actually doing so.

2.5 Alternatively, if Article 88F(2)(b) is intended to have some other effect, it would be helpful if HMT could confirm the relevant policy rationale and assess whether any of the risks we raise above might nonetheless still be applicable, such that a different approach is appropriate.

3. DEFINITION OF A QUALIFYING STABLECOIN

Electronic money

3.1 There has been a policy decision to place a bright line between the QS and electronic money regimes (in contrast to the approach taken in the EU's Markets in Crypto-Assets Regulation (**MiCA**)). This has been attempted by excluding electronic money from the definition of a QCA, as well as excluding a QS from the concept of stored monetary value in regulation 3ZA of the Electronic Money Regulations 2011 (**EMRs**).

3.2 Unfortunately, this structure makes the definitions circular. The steps a firm would need to go through to establish its regulatory classification would be as follows:

(a) Article 88G (meaning of QS) points to Article 88F (meaning of QCA).

(b) Article 88F excludes electronic money, thus pointing to regulation 2 of the EMRs.

(c) Regulation 2 of the EMRs must be read with regulation 3ZA.

(d) Regulation 3ZA excludes a QS from stored monetary value.

(e) This points the firm back to Article 88G.

3.3 In order to avoid this circularity problem in the drafting, we suggest that Article 88G(1) be amended to refer only to a "cryptoasset" (as opposed to a *qualifying* cryptoasset). At that point the exclusions in Article 88F and regulation 3ZA work as intended. It might also be appropriate then to incorporate into, and set out in, the definition of QS in Article 88G, the fungibility and transferability requirements of Article 88F(1) (suitably modified to avoid the issue we have identified above in relation to what is currently proposed in new Article 88F(2)(b)).

Tokenised deposits

3.4 There is also an issue with the approach taken to tokenised deposits. Under the proposed new Article 88G(2), the definition of QS excludes a cryptoasset that comprises or represents a claim for the repayment of a deposit received by an authorised person with Part 4A permission to accept deposits. We understand that the policy intention behind this drafting is to exclude tokenised deposits from the definition of a "qualifying stablecoin".

3.5 However, the existing drafting appears to mean that a tokenised deposit representing a claim on a deposit received by a non-UK bank (meaning one without Part 4A permission for accepting deposits) would not benefit from this exclusion and, therefore, could still constitute a qualifying stablecoin (and, therefore, a qualifying cryptoasset under Article 88F(3)). We had understood HMT's policy intention to be that all tokenised deposits were intended to be excluded from the scope of a qualifying cryptoasset for these purposes, whereas the existing drafting would mean that relevant activities carried on in relation to certain forms of tokenised deposits could still require Part 4A permissions for the new cryptoasset regulated activities.

3.6 We would, therefore, suggest that the exclusion in Article 88G(2) should be widened to cover a cryptoasset that comprises or represents a claim on a deposit received by a non-UK bank (if necessary, qualified by reference to the non-UK bank having any required authorisation to accept deposits in the jurisdiction in which the deposit is deemed to be accepted).

4. DEFINITION OF A SPECIFIED INVESTMENT CRYPTOASSET

4.1 Under the proposed amendments to the definitions in Article 3(2), a "**specified investment cryptoasset**" is defined as:

> "*a cryptoasset that is a specified investment, as specified within Part 3 (specified investments), including where the cryptoasset is a right to or an interest in such a specified investment within Article 89 (rights to or interests in investments)*".

4.2 In accordance with s.417(1) FSMA, the definition of a "**cryptoasset**" for these purposes is:

> *"any cryptographically secured digital representation of value or contractual rights that—*
>
> *(a) can be transferred, stored or traded electronically, and*

(b) that uses technology supporting the recording or storage of data (which may include distributed ledger technology)".

4.3 The combined effect of these definitions is that a "specified investment cryptoasset" is defined very broadly, covering (among other arrangements) any cryptographically secured digital representation of contractual rights that can be transferred or traded electronically and that uses technology supporting the storage of data.

4.4 The definition of a "**relevant specified investment cryptoasset**" then operates as a subset of specified investment cryptoassets, being a specified investment cryptoasset that is a security or contractually based investment.

4.5 In practice, it appears that the "specified investment cryptoasset" and "relevant specified investment cryptoasset" definitions are potentially wide enough to capture, for example, interests in uncertificated securities that are held through central securities depositories (CSDs), where the CSD employs cryptographic authentication or security methods in connection with the storage or transfer of such securities (represented in electronic, i.e. digital, form). It is common for CSDs to use cryptographic authentication methods to secure the transfer of uncertificated securities by holders of those securities, including public and private security keys, such that the uncertificated securities (represented in electronic, i.e. digital, form) might be considered to be "cryptographically secured digital representations" of the contractual rights attaching to the relevant securities. We assume that HMT did not intend to capture such arrangements within the definition of a "specified investment cryptoasset" or a "relevant specified investment cryptoasset" and for such uncertificated securities to continue to remain subject to the existing regulatory regime.

4.6 Even if uncertificated (registered) securities fall outside the relevant specified investment cryptoasset definition in themselves, CSDs may also be providing services directly in relation to tokenised securities (i.e. where the underlying security is "linked" or "stapled" to a crypto-token) that would clearly fall within the definition of a relevant specified investment cryptoasset.

4.7 The effect of s.285(3D) FSMA is to exempt a recognised CSD from the general prohibition in respect of any regulated activity carried on for the purposes of, or in connection with, relevant services under the assimilated law version of CSDR. While this provision would operate to exempt the CSD itself from the requirement for Part 4A authorisation in relation to relevant securities settlement activities carried out in relation to specified investment cryptoassets, there is nonetheless a risk of unintended effects for the business models of certain CSDs where affiliated entities (which do not themselves benefit from the s.285 FSMA exemption) may be connected to the provision of settlement services.

4.8 One such issue may arise in connection with nominee and related structures used by a recognised CSD for the purpose of holding (as custodian) relevant specified investment cryptoassets. . The proposed new regulated activity in Article 9O(1)(a) of safeguarding of qualifying cryptoassets and relevant specified investment cryptoassets on behalf of another is broadly defined. For these purposes, Article 9O(2)(a) states that the activity of "**safeguarding**" is carried on in circumstances where:

"*a person ('C') has control of the cryptoasset through any means that would enable C to bring about a transfer of the benefit of the cryptoasset to another person, including to C*".

4.9 The concept of control for these purposes is defined non-exhaustively in Article 9O(3) as including: (i) holding or storing the means of access (or part of it) to the cryptoasset; or (ii) appointing another person to hold or store the means of access (or part of) under an arrangement operated by C. However, as this definition is non-exhaustive, it appears that if there are other means by which a person can bring about a transfer of the benefit of a cryptoasset to another person, this would still constitute control for the purposes of the Article 9O(1) safeguarding activity. Accordingly, where a nominee (and any other wholly-owned subsidiary of a CSD) is used to hold e.g. overseas relevant specified investment cryptoassets as part of a CSD-CSD link to enable UK investors to settle transactions in foreign securities), the nominee entity (and any other relevant entity connected to the CSD used as part of the arrangements) - which do not themselves benefit from the exemption in s.285(3D) FSMA - are likely to be considered to be carrying on the Article 9O(1) safeguarding activity.

4.10 Under the existing RAO framework in relation to securities, a nominee (or other CSD-connected) entity may typically avoid the need for Part 4A authorisation because:

4.10.1 the nominee (or such other entity) may only be safeguarding the relevant asset, but not administering it (and Article 40(1) is clear that a person must perform *both* safeguarding and administering to fall within scope of the regulated activity);

4.10.2 as the nominee will normally be acting as a bare trustee, Article 66(4) contains an exclusion from the Article 40 safeguarding activity for a person acting in the capacity of a trustee, unless that person holds himself out as providing the Article 40 safeguarding activity; and/or

4.10.3 the exemption in Article 41 provides that the nominee (and any other relevant connected entity performing custody functions) does not carry on the Article 40 safeguarding and administering activity if a "qualifying custodian" undertakes to the owner of the assets that the custodian will have the same responsibility for those assets as if it were safeguarding them itself, and the qualifying custodian does so in the course of carrying on in the UK safeguarding activity that would fall within Article 40. Under Article 41(2)(b) (read together with the definition of an "exempt person" in s.417 FSMA), a "qualifying custodian" would include a CSD that benefits from the s.285(3D) FSMA exemption. We discuss the implications of this further, in relation to the current drafting of the exclusions for the "safeguarding" activity in Article 9O, in Section 6 of this submission. We suggest in that section potential solutions to the legal uncertainties presently created by the failure to include an appropriate exclusion for CSD-related nominees and other entities

performing custody-related functions in relation to relevant specified investment cryptoassets.

4.11 In addition, the breadth of the definition of cryptoasset raises the risk that it captures cryptographically secured registers or other records evidencing proprietary interests (rather than embodying the asset itself). These are arrangements under which crypto-tokens are used merely as part of a register or record of entitlements. We would recommend that s.417(1) FSMA be amended to clarify that the use of cryptographically secured records to maintain a register of title or other record of securities does not in and of itself result in the securities being regarded as cryptoassets.

5. TERRITORIAL SCOPE

5.1 Based on the explanation in paragraphs 2.11 and 2.12 of HMT's Policy Note, we understand HMT's policy intention in relation to the territorial scope of the proposed new framework to be as follows (assuming, in each case, that no relevant exclusion applies):

5.1.1 a UK or non-UK firm would need a Part 4A permission to carry on any of the following activities where the firm is dealing directly or indirectly with a UK consumer (unless the firm is dealing with the UK consumer via an intermediary acting as a qualifying cryptoasset trading platform or dealing in qualifying cryptoassets as principal, in either case where the intermediary has the appropriate Part 4A permission):

(a) operating a qualifying cryptoasset trading platform (Article 9T);

(b) dealing in qualifying cryptoassets as principal (Article 9U);

(c) dealing in qualifying cryptoassets as agent (Article 9X);

(d) arranging deals in qualifying cryptoassets (Article 9Z);

5.1.2 a non-UK firm carrying on any of the activities in paragraph 5.1.1 above in relation to UK clients or counterparties who are not consumers (termed "UK institutional customers" in the Policy Note) would not require Part 4A authorisation, provided that the UK client or counterparty is not acting as an intermediary between the non-UK firm and UK consumers;

5.1.3 a UK or non-UK firm will need a Part 4A permission to carry on either of the following activities where it is doing so in the UK or on behalf of a consumer in the UK:

(a) safeguarding qualifying cryptoassets and relevant specified investment cryptoassets (Article 9O) unless the firm carries out the activity in question at the direction of a person who is authorised to carry out that activity; or

(b) qualifying cryptoasset staking (Article 9Z7);

5.1.4 a UK or non-UK firm issuing qualifying stablecoin (Article 9M) will need Part 4A permission if the activity is carried on from a UK establishment; and

5.1.5 as is set out in paragraph 2.12.2 of the Policy Note, the distinction between consumers and institutional customers is only relevant to the jurisdictional analysis needed for overseas firms when considering s.418 FSMA. This means that UK firms (i.e. where there is no need to analyse geographic application) will need a Part 4A permission irrespective of the nature of their UK customers.

5.2 In practice, assuming that we are correct on the policy intention, it is not clear to us that HMT's current proposed drafting will fully achieve (what we understand to be) the intended effect above.

Territorial scope of dealing, arranging and operating trading platform activities

5.3 It appears that to achieve the intended outcomes in paragraphs 5.1.1 and 5.1.2 above, HMT has added the new provision in s.418(6A) FSMA. In our view, the existing drafting approach may not achieve HMT's policy intention in this regard.

5.4 The addition of s.418(6A) FSMA would definitively scope *into* the Part 4A regime a non-UK firm performing any of the relevant activities directly or indirectly with a UK consumer (except where a relevant authorised intermediary is acting as a qualifying cryptoasset trading platform or dealing in qualifying cryptoassets as principal). However, it does not follow that an overseas firm performing the relevant activity in relation to a UK person who is not a consumer would automatically fall outside of the requirement for FCA authorisation.

5.5 This is because where a firm falls within one or more of the cases specified in s.418 FSMA, it is to be treated as carrying on a regulated activity in the UK (and therefore, would normally need a Part 4A permission, in the absence of an available exclusion) even though the activity in question would not otherwise be regarded as carried on in the UK. The reverse is not true – i.e. a firm that falls outside of all the cases in s.418 FSMA is not for that reason alone to be treated definitively as *not* carrying on a regulated activity in the UK.

5.6 As a result, the question of whether a non-UK firm would need Part 4A permission to carry on any of the relevant dealing, arranging or operating a cryptoasset trading platform activities is not addressed by s.418 FSMA. Instead, this becomes a question of interpreting the inherent territorial scope of each underlying regulated activity. Except in cases where the legislative definition of the regulated activity expressly incorporates a territorial component (such as in the proposed Article 9M issuing activity, discussed below), there is often a lack of clarity around when an activity is to be viewed as carried on in the UK or not.

5.7 For many of the activities in the current FSMA regime (including, for example, superficially analogous arranging and dealing activities in relation to securities and contractually based

investments in Articles 14, 21 and 25), there is typically a lack of definitive case law and limited regulatory guidance on the question of territoriality. In any case, regulatory guidance in itself does not bind the courts, even though in many cases, it may be highly persuasive.

5.8 In our view, it would be unsatisfactory to rely on existing widely held views on the territorial scope of equivalent regulated activities in the RAO to achieve the intended policy outcomes (as set out in paragraphs 5.1.1 and 5.1.2) in this context. This is because:

5.8.1 Although certain views are widely held, they are not necessarily *universally* held and therefore legal certainty will not be achieved.

5.8.2 Those views are largely based on historical guidance from regulators (including regulators which pre-dated the FCA) and, therefore, could be modified by future FCA guidance, leaving too much regulatory discretion to determine a fundamental policy element of the regime which is better reserved to HMT.

5.8.3 The consequences of breaching the general prohibition in s.19 FSMA are significant, including potential criminal liability and a lack of enforceability of legal agreements, so that any material degree of uncertainty may have a chilling effect on firms' willingness to engage in cryptoasset business with a UK nexus.

5.8.4 Given that the cryptoasset regulated activities are new, it does not automatically follow that existing interpretations of the territorial scope of apparently similar existing regulated activities can and should be applied to the new activities.

5.8.5 It is not clear that existing interpretations of the territorial scope of certain regulated activities would in any case achieve HMT's apparent intended policy outcome. For example, although there is limited guidance, the Article 21 dealing as agent activity is often considered to be carried on where acceptance of the relevant contract occurs (by analogy with current FCA guidance in PERG 5.12.8G in relation to contracts of insurance). If it is assumed that this approach applies by analogy to the Article 9X (dealing in qualifying cryptoassets as agent) activity, this would mean that an overseas firm dealing as agent from outside the UK on behalf of an overseas counterparty would be treated as carrying on that activity in the UK where a UK institutional investor is deemed to accept the relevant offer in the UK. S.418 FSMA does not change this analysis because it applies only in cases where a regulated activity would not otherwise be treated as carried on in the UK. We understand that this sort of situation would not be the outcome HMT is seeking.

5.9 Given that HMT has a clear policy intention as regards territorial scope in this context, and in light of the importance of certainty in relation to when digital assets will be within the

scope of UK regulation, we consider that HMT should legislate for a clearer territorial scope for each regulated activity, rather than adopting the partial approach of simply amending s.418 FSMA. The easiest way to achieve a sufficient degree of certainty (while remaining broadly consistent with the approach used elsewhere in the RAO) would be to adapt the existing Article 72 overseas persons exclusion. This would provide a clear "safe harbour" according to which non-UK firms dealing with UK counterparties can have certainty that they are outside the requirement for Part 4A authorisation. Where necessary, the application of the Article 72 exclusion in relation to cryptoasset activities could be adapted to scope into regulation relevant activities carried on by an overseas person with a UK consumer.

Territorial scope of cryptoasset custody and cryptoasset staking activities

5.10 To achieve the intended outcome in paragraph 5.1.3 above, we understand that HMT is proposing to add s.418(6C) to FSMA. For similar reasons to those stated above, it is not necessarily clear that this will achieve the intended policy outcome, assuming that HMT does not intend to capture an offshore firm providing cryptoasset custody or cryptoasset staking services from an establishment outside the UK to a UK institutional customer.

5.11 We recognise that if the "traditional" view of the territorial scope of the analogous safeguarding activities (i.e. safeguarding and administering investments, and arranging safeguarding and administration of investments) in Article 40 applies to the new proposed Article 9O cryptoasset safeguarding activities, a non-UK firm holding or storing the means of access to a cryptoasset outside the UK may be considered not to be carrying on the relevant activity in the UK. As a result, such a firm would not need Part 4A permission for the Article 9O activity (except to the extent it fell within s.418(6C) FSMA because it was safeguarding or arranging safeguarding directly or indirectly for a UK consumer and not doing so at the direction of another person authorised to carry on the Article 9O activity).

5.12 However, as noted above, there is no guarantee that a regulator or court would necessarily adopt the "traditional" view. This is particularly the case given that the nature of the new Article 9O activity is fundamentally different from the traditional safeguarding of securities or contractually based investments, being defined by reference to control over the cryptoasset through any means enabling the person to bring about a transfer of the benefit for the cryptoasset to another person.

5.13 Therefore, while we acknowledge that the current overseas persons exemption in Article 72 does not apply to the Article 40 safeguarding activity, for reasons of legal certainty in circumstances where there are novel regulated activities defined by reference to new concepts, we consider that it would still be desirable in practice to modify Article 72 to provide a "safe harbour" where a non-UK firm is providing or arranging safeguarding of qualifying cryptoassets or relevant specified investment cryptoassets for a UK institutional customer.

Territorial scope of issuing activity

5.14 We agree that Article 9M is only engaged where one or more of the activities constituting issuing (i.e. those activities listed in Article 9M(2)) is carried on from a UK establishment. This is because it is an integral part of the drafting of Article 9M(1) and 9M(2) that the activity is carried on in the UK by a person *established* in the UK.

5.15 We would strongly recommend that – if HMT is unwilling to extend the application of Article 72 (as proposed in paragraph 5.20 below) – there needs to be a statutory definition for the purposes of Article 9M of "established in the United Kingdom". Failure to do so leaves the geographical scope of the perimeter unclear, which will also directly increase the reluctance of UK firms (such as custodians or asset managers) to deal with overseas stablecoin issuers.

5.16 In addition, we consider that in limiting Article 9M only to activities carried on from the UK by a person established in the UK, the current drafting approach risks putting UK stablecoin issuers at a significant competitive disadvantage to overseas stablecoin issuers targeting UK customers. This is because it is likely that UK issuers will become subject to substantial regulatory requirements imposed by the FCA, whereas overseas issuers would not be subject to the same requirements (and, depending on their jurisdiction, may not necessarily be subject to any regulatory requirements at all).

5.17 In addition, it could be said to be unfortunate that the Policy Note does not address the intra-group deeming provisions in Article 9M(5)(a). We note that there is no territorial qualifier in this provision. We interpret this provision, in practice, as meaning that (for example) a firm established in the UK, which is a member of the same group as an overseas stablecoin issuer (the "**sister issuer**"), will be deemed to be carrying on the regulated activity of issuing a qualifying stablecoin if it carries on any of the activities listed in Article 9M(2). In fact, this could even be the case where the sister issuer does not even intend for its stablecoins to be purchased by clients in the UK – the only counter-argument seems to be whether or not this was "issuing a qualifying stablecoin **in the United Kingdom**" (our emphasis) for the purposes of Article 9M(1). This potentially captures a wider range of corporate structures that was envisaged, and our view is that the market has instead focussed on the high-level policy expressed in paragraph 2.12.4 of the Policy Note.

5.18 The current drafting seems to provide a wide right of access for those overseas issuers to UK customers. In particular, Article 9M(2) defines the issuing activity by reference to whether a person is established in the UK (in addition to the requirement in Article 9M(1) that the activity must take place in the UK). This appears to mean that a person may be carrying on an issuing activity in the UK without falling within Article 9M, provided that the relevant person is not established in the UK. Although the concept of being "established" in the UK for these purposes is not defined in the drafting, it seems likely that this could be interpreted to require a degree of permanence that exceeds merely being temporarily present in the UK. As a result, it appears that representatives of an overseas issuer could temporarily visit the UK to offer qualifying stablecoins to UK customers (including UK consumers) without requiring Part 4A permission for the Article 9M activity.

5.19 The other cryptoasset regulated activities are also unlikely to be engaged. The Article 9Z arranging activity does not include arrangements to which the overseas firm is itself a party due to the effect of Article 9Z4, and the Article 9U dealing as principal activity specifically excludes any activity falling within Article 9M, due to the effect of Article 9W(4)(a) – although we acknowledge there is material uncertainty and ambiguity as to whether Article 9W(4)(a), as well as Articles 9Y(3)(a) and 9Z6(4)(a), are intended to cover non-UK issuers or whether such issuers may, for example, still be "dealing" in a QS when they perform redemption functions in relation to the QS, i.e. it is unclear whether Article 9M is intended to be an exhaustive expression of when the carrying on of an issuance-related function in relation to a QS falls in-scope of the regulatory perimeter, or whether Articles 9U, 9X and 9Z continue to operate in respect of a non-UK issuer performing issuance-related functions for a QS. The remaining activities are unlikely to be relevant where it is the issuer offering its own stablecoins directly to a customer (whether a consumer or not). The Article 64 (agreeing) activity will not apply to Article 9M issuing under HMT's proposals so that entering into an agreement in the UK to issuer the relevant stablecoin would not be a regulated activity either.

5.20 In our view, it would be more appropriate for the Article 9M issuing activity to be capable of applying to stablecoin issuance that takes place both in or outside the UK, but subject to the overseas persons exclusion in Article 72 (modified, as necessary, to cover the Article 9M activity) – and, if Article 9M is intended to be an exhaustive expression of when issuance-related activities are intended to fall within scope of the RAO, extending to the dealing (principal and agent) and arranging regulated activities to the extent they might otherwise be engaged by the performance by a non-UK issuer of the issuance-related functions set out in Article 9M. This would allow overseas issuers to offer stablecoins to UK customers without requiring Part 4A authorisation where they fall within the definition of an "overseas person" (and therefore are not carrying on their activities, or offering to do so, from a permanent place of business maintained in the UK), subject to the offer being a "legitimate approach" – i.e. not solicited by the issuer, or solicited in a way that complies with the financial promotions restriction in s.21 FSMA.

6. SAFEGUARDING OF QUALIFYING CRYPTOASSETS AND RELEVANT SPECIFIED INVESTMENT CRYPTOASSETS

6.1 The new cryptoasset safeguarding activity in Article 9O(1)(a) refers to safeguarding of qualifying cryptoassets or relevant specified investment cryptoassets on behalf of another. Article 9O(2)(b)(iii) defines the concept of "on behalf of another" as including where the other person has a right against the firm for the return of a qualifying cryptoasset or relevant specified investment cryptoasset (as distinct from the other person having legal and/or beneficial title, which is referenced separately in Article 9O(2)(b)(i) and (ii)).

6.2 As drafted, it would therefore appear that the new safeguarding activity could include circumstances in which a person transfers legal and beneficial title to the firm and has only a contractual right for the return of the asset at some future date. In turn, it appears that a firm that is engaged in cryptoasset borrowing, or that took control of a cryptoasset as part of a collateral arrangement under which full ownership is transferred to that person,

would be carrying out the Article 9O(1)(a) safeguarding activity and would, therefore, need a Part 4A permission for that activity. It is unclear whether this is intended, and it may potentially interfere with the use of cryptoassets (including QS) as collateral in the future. In practice, it is likely to mean that a great deal of analysis will be needed whenever anyone borrows a cryptoasset, to establish whether this is being carried on by way of business. It is also somewhat at odds with the statement in paragraph 2.9 (second bullet) of the Policy Note, that the Article 9U dealing as principal activity "is also intended to capture cryptoasset lending and borrowing services."

6.3 In addition, the new safeguarding activity in Article 9O consists of a single activity – i.e. having control over the cryptoasset through any means enabling the person to bring about a transfer of the benefit of the cryptoasset to another person. As such, where a nominee (or other relevant) entity has such control because it stores a private cryptographic key (or part of one) in relation to the cryptoasset on behalf of another, it will be within scope of Article 9O(1)(a).

6.4 As a result, there is no longer any concept of administration forming a necessary part of the new regulated activity.

6.5 We are concerned that the current drafting of Article 9O fails to recognise an important distinction between two types of custody model that may be relevant to QCAs and relevant specified investment cryptoassets. These are:

6.5.1 First, traditional custody models, for the safeguarding and administering of an asset - under which the custodian holds legal or beneficial title to cryptoassets belonging to a client (we refer to this activity as "**holding control**" by a custodian of the relevant asset).

6.5.2 Second, custody models solely for the safeguarding (but not administering) of an asset – under which the custodian is not vested with any legal or beneficial title to cryptoassets belonging to the client, but merely safeguards the private cryptographic key relating to the asset (in order to store, hold and transfer the asset) in circumstances that do not involve the custodian carrying on the "safeguarding and administering" activity outlined in paragraph 6.5.1 above (we refer to this activity as "**non-holding control**" by a custodian of the relevant asset). This latter model was expressly identified as long ago as in the original Call for Evidence of February 2023 (see Table 8.A).

6.6 We assume, from the approach laid out by HMT to date, that capturing non-holding control is HMT's settled policy, taking into account the view that the risks arising out of, or in connection with, a holding control custody arrangement may be different from those arising out of, or in connection with, a non-holding control custody arrangement. The first type of arrangement creates materially the same risks as arising in connection with the safeguarding and administering of traditional financial instruments.

6.7 As such, and on the basis of the "same risk, same regulatory outcome" principle, we believe that holding control of a relevant cryptoasset by a custodian should be regulated

in the same way as holding control of a traditional financial instrument. This means that it would be appropriate for the draft statutory instrument either (a) to bring qualifying cryptoassets and relevant specified investment cryptoassets within scope of Article 40, or (b) to establish a new Article 9O activity (consistent with what is contemplated by new Article 40(4)) for the "safeguarding and administering" of such cryptoassets drafted in exactly the same terms as Article 40.

6.8 In addition, in recognition of the fact that non-holding control of a cryptoasset by a custodian may create different risks to those associated with holding control, we would suggest that a separate and new regulated activity be established in the draft statutory instrument for the non-holding control of a qualifying cryptoasset or a relevant specified investment cryptoasset. This would establish a "regulatory hook" for, for example, the separate regulation of such non-holding control arrangements in a similar way to other "mandate" arrangements (not constituting holding control or safeguarding and administering) under CASS 8 of the FCA Handbook.

6.9 This policy outcome might be achieved (depending upon how HM determines it best to recognise "holding control" custody arrangements) by setting out in Article 9O a separate regulated activity in the following terms:

> *"the safeguarding by a person ("C") of the technological means of access to a qualifying cryptoasset or relevant specified investment cryptoasset on behalf of another person that enables C to transfer title to the cryptoasset, but where such safeguarding is not an activity which is, or forms part of, a regulated activity specified in [Article 40][Article 9O(1)]".*

6.10 The term "technological means of access" might be defined by reference to (i) a private cryptographic key to a cryptoasset, (ii) one or more parts of that private cryptographic key or (iii) any other personalised device or personalised set of procedures used by a person to transfer title to a cryptoasset. We consider it necessary to include an exhaustive, technology-referenced definition to provide the required level of legal and regulatory certainty for participants in the digital assets markets, as well as to avoid, for example, arrangements such as those constituted by a power of attorney (without more) constituting relevant "means of access".

6.11 The draft statutory instrument would also make "arranging for one or more persons to carry on" the non-holding control (safeguarding) activity a regulated activity.

6.12 The new Article 9P has some similarities with the exclusion in Article 41, but is narrower in scope. In particular, under Article 9P(1)(a), the arrangements pursuant to which the nominee (or other relevant entity) would be holding/controlling the relevant cryptoassets must be operated by an *authorised* cryptoasset custodian (which, under Article 3, is defined as an authorised person with a Part 4A permission to carry on the regulated cryptoasset safeguarding activity in Article 9O(1)(a)). This is more limited in scope than the equivalent concept of a "qualifying custodian" in Article 41, which is defined in Article 41(2)(b) as including an exempt person acting in the course of business comprising a regulated activity in relation to which he is exempt. The effect of this narrowing is that

nominees (and other associated entities) of a recognised CSD could benefit from the Article 41 exclusion, but would not be able to benefit from the Article 9P exemption. We would therefore recommend that Article 9P should be expanded to include arrangements operated by an exempt person acting in the course of an exempt activity – ideally, by adopting the "qualifying custodian" concept as defined in Article 41(2).

6.13 Article 9S(2) contains a general exclusion from the Article 9O(1)(a) safeguarding activity where the relevant person does not hold themselves out as engaging in the business of providing a service in relation to in-scope cryptoassets. We note that this exclusion is potentially wider than the equivalent existing exclusion in Article 66(4), in that it does not require the person to be acting as a trustee or personal representative. It may be possible for a nominee (or other relevant) entity to rely on this provision, although this could also depend upon any future guidance given by the FCA on the interpretation of "holding out". Accordingly, we consider that it would still be desirable to amend Article 9P in the manner indicated above to provide an alternative mechanism by which a nominee (and another associated entity) of a recognised CSD could be excluded from the requirement for Part 4A authorisation when holding relevant specified investment cryptoassets.

6.14 We suggest that the approach for the holding and non-holding control of QCAs and relevant specified investment cryptoassets should mirror the approach taken in the existing Article 41 for traditional financial instruments. The category of "authorised cryptoasset custodian" that may undertake responsibility to the person on whose behalf the qualifying cryptoasset or relevant specified investment cryptoasset is being safeguarded for the purposes of Article 9P should be widened to include the additional persons covered within the category of "qualifying custodian" in Article 41. In addition, the requirement that the custodian be grouped with the relevant person who would otherwise be carrying on safeguarding, which is not a requirement of the current exemption contained in Article 41 (there is a separate group exemption in Article 69), should also be omitted from the exclusion. As a general principle, we see no reason why all of the other exclusions available to the safeguarding and administration of traditional financial instruments should not also apply to the new Article 9O regulated activity – and the draft statutory instrument should be amended accordingly.

7. STATUTORY IMMUNITY FOR REGULATORY FUNCTIONS OF CRYPTOASSET TRADING PLATFORMS

7.1 In our view, HMT should properly extend the existing statutory immunity contained in s.291 FSMA (or create a similar separate provision) in relation to the regulatory functions of a recognised body to the operators of a qualifying cryptoasset trading platform (i.e. persons carrying on the new proposed Article 9T activity).

7.2 The FCA's DP24/4 proposes that a number of regulatory functions that are performed by the FCA in relation to traditional financial instruments (for example, the receipt and assessment of STORs) will, in relation to QCAs, be required to be performed by the CATPs.

7.3 This means that certain public law obligations will be imposed on CATPs in relation to which, consistent with the principle of "same risk, same regulatory outcome", they need

to receive the same statutory protections as are extended to recognised bodies under Part XVIII FSMA when performing public functions.

8. TREATMENT OF PHYSICAL BACKING ASSETS FOR ASSET-BACKED TOKENS THAT ARE NOT QUALIFYING STABLECOIN

8.1 Although it is not discussed in the Policy Note, the amendment to Article 98 (which deals with the application of s.137B FSMA) has widened the FCA's power to make rules imposing a statutory trust over backing assets for qualifying stablecoins that are not fiat currency. This is essential given the structure in Article 88G.

8.2 However, we do not consider that this drafting goes far enough. MiCA has specific provisions for "asset-referenced tokens", defined as " a type of cryptoasset that is not [a qualifying stablecoin in UK parlance] and that purports to maintain a stable value by referencing another value or right or a combination thereof, including one or more official currencies". For ease, we adopt the term "**ART**" in this section of our response to refer to such tokens.

8.3 Cryptoassets structured in that way will be classified under the draft statutory instrument as falling within the definition of QCA but outside the definition of QS. This means that the FCA's powers under s.137B FSMA are inadequately extended in two ways.

8.4 First, there is no ability to impose the statutory trust in the FCA's Client Assets Sourcebook (**CASS**) to backing assets for ARTs, because they are not QS.

8.5 Secondly, this also means that the FCA has no power to recognise the use, for backing assets of ARTs, of structures other than trusts. This would be important to issuers of ARTs (which would arguably include Tether Gold and Paxos Gold outside the UK, for example) because, for cryptoassets backed by physical commodities, there are many valid commercial and operational reasons to prefer that the backing assets are held using bailment rather than a trust.

8.6 The FCA would be unable to resolve this problem using its powers alone, which is why it should be dealt with in statute. We recommend amending the drafting of Article 98 to permit this.

We are happy to discuss these comments further in whatever format HMT might find helpful.

Travers Smith LLP

23 May 2025