



Financial Services & Products ADVISORY ■

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UK Treasury Moves Forward with Plans to Regulate Stablecoins for Payments

Earlier this month, HM Treasury published its UK Regulatory Approach to Cryptoassets, Stablecoins, and Distributed Ledger Technology in response to its January 2021 consultation and call for evidence.

The response confirms the government's intention to bring activities that issue or facilitate the use of stablecoins used as a means of payment into the UK regulatory regime.

Key Proposals

Stablecoins used as a means of payment to be brought within existing regulations

- The government intends to regulate activities that issue or facilitate the use of stablecoins as a means of payment, primarily by amending the existing Electronic Money Regulations 2011 and the Payment Services Regulations 2017.
- The government will amend the definition of 'e-money' and introduce a new definition for a 'payment cryptoasset' (or something similar) that will bring into scope
any cryptographically secured digital representation of monetary value which is, among other things, stabilised by reference to one or more fiat currencies and/or is issued and used as a means of making payment transactions.
- The definition of 'payment cryptoassets' refers to fiat-backed stablecoins. At this stage, the government has intentionally excluded algorithmic stablecoins or those that may be linked to assets other than fiat currency (e.g., commodities).
- Authorisation under the Electronic Money Regulations 2011 and the Payment Services Regulations 2017 requires entities to be located in the UK, and it is unclear whether issuers of payment cryptoassets will be required to do the same. Further consideration and consultation on this issue is expected.

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Extension of legislation to stablecoin custodians and wallet providers

- The government will also bring firms that ‘provide services to custody or arrange the custody of stablecoins used as a means of payment on behalf of customers’ within the UK regulatory landscape, meaning that they will need to be authorised by the Financial Conduct Authority (FCA).
- The government will set out in legislation how that new activity will be brought within the regulatory regime and the FCA’s powers.
- The FCA will also establish a detailed set of regulatory rules that apply to stablecoin custodians, covering for example: prudential and organisational requirements, reporting requirements, conduct of business requirements, operational resilience, custody/safeguarding requirements, and consumer protections.

Extension of the application of Part 5 of the Banking Act 2009

- Part 5 of the Banking Act 2009 deals with the Bank of England’s oversight of payment systems that are of systemic significance to the UK.
- The government plans to extend the applicability of Part 5 to include stablecoin activities in cases where the risks posed have the potential to be ‘systemic’ and therefore require supervision by the Bank of England.

Extension to the scope of the Financial Services (Banking Reform) Act 2013

- The Financial Services (Banking Reform) Act 2013 established the roles, responsibilities, and powers of a payment systems regulator (a new regulator charged with increasing competition in the payments sector).
- The government has stated that the scope of the Financial Services (Banking Reform) Act 2013 will be extended to apply to payment systems facilitating the transfer of new types of stablecoin to ensure that such payment systems are also subject to appropriate competition regulation by the payment systems regulator. Further clarification on how the legislation will operate is to be provided.

Financial market infrastructure sandbox

- The government recognised the substantial benefits and transformative impact that could be delivered by distributed ledger technology (DLT) when adopted in financial market infrastructures (FMIs).
- The government is therefore developing an FMI sandbox (to be up and running in 2023) to support firms wanting to innovate, including by using these technologies to provide FMI services.
- Under the FMI sandbox, participants can request exemptions from or modifications to existing legislation to facilitate testing of DLT in FMIs and to enable the UK authorities to gain a better understanding of the legislative changes necessary to accommodate DLT.
- A further consultation with industry is expected before HM Treasury introduces secondary legislation to set out the detailed legislative framework of the FMI sandbox.

Broader cryptoassets

- HM Treasury is continuing to assess the appropriate regulatory response to broader cryptoassets (i.e., beyond just stablecoins used as a means of payment).
- The government intends to continue to monitor this fast-growing area and will work with the UK financial regulators and industry to consider appropriate future regulation.
- HM Treasury will consult later in 2022 on its proposed approach.

Further Proposals

In addition to these proposals, the FCA also announced they will be organising the first of a series of 'crypto-sprints' next month involving industry experts. These sprints are intended to inform FCA policy thinking in real time, and participants will be tasked with considering some of the legal, technical, and regulatory challenges the industry faces and suggesting solutions the government will then seek to take forward.

It was also announced that the government will be establishing a high-level industry group, the Cryptoasset Engagement Group, which will comprise senior representatives from regulatory authorities and the industry to help guide the government on issues involving cryptoassets.

Finally, the Chancellor has asked the Royal Mint to create a non-fungible token (NFT) to be issued by the summer, which was referred to by Economic Secretary to the Treasury John Glen as being 'an emblem of the forward-looking approach we are determined to take'.

All these initiatives follow other developments affecting cryptoassets over the past few years, including bringing cryptoasset services providers within the UK anti-money laundering regime and more recently introducing proposals to bring cryptoassets within the UK's financial promotions regime.

In Glen's words, the UK is seeking to be 'a global hub – the very best place in the world to start and scale crypto-companies'.

We shall await the legislation implementing the new regulatory regime for stablecoins, which will be introduced 'when Parliamentary time allows' and will provide further updates as these proposals develop.

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