

UK Regulators Publish Updates for the Regulation of Fiat-Backed Stablecoins

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On 6 November 2023, the Bank of England (**BoE**) published a discussion paper on the “Regulatory Regime for Systemic Payment Systems Using Stablecoins and Related Service Providers” (the **Discussion Paper**). The Discussion Paper has been published alongside:

1. the Financial Conduct Authority (**FCA**) discussion paper “Regulating Cryptoassets Phase 1: Stablecoins”, detailing their regulatory approach to stablecoin issuers and custodians (**DP23/4**);
2. a letter from the Prudential Regulation Authority (**PRA**) to bank chief executive officers on “Innovations in the Use by Deposit-takers of Deposits, E-money and Regulated Stablecoins” (the **Letter**); and
3. a “Cross-authority Roadmap on Innovation in Payments” (the **Roadmap**), issued by the BoE, PRA and FCA (jointly, the **Regulators**)

(the Discussion Paper, DP23/4 and the Letter jointly, the **Publications**).

With the Publications, the Regulators aim to provide clarity as to which regulatory structure each form of money and money-like instrument falls under, with regulatory boundaries between each framework clearly established. The Publications follow a policy paper published by HM Treasury (**HMT**) on 30 October 2023 which contained an update on its plans for the regulation of fiat-backed stablecoins (the **Policy Paper**).

The Policy Paper

The Policy Paper confirmed HMT's intention to legislate to bring certain fiat-backed stablecoins within the remit of the BoE, the FCA and the Payment Systems Regulator (**PSR**). Most notably, the Policy Paper confirms that HMT:

1. will bring activities relating to fiat-backed stablecoins into the FCA's regulatory perimeter via secondary legislation;
2. intends to define fiat-backed stablecoins as a cryptoasset that seeks or purports to maintain a stable value by reference to a fiat currency and by holding fiat currency, in whole or in part, as backing. HMT confirms that this definition will not:
 - a. be limited to particular currencies;
 - b. be limited to single currency stablecoins;
 - c. include algorithmic or cryptobacked stablecoins;
 - d. include commodity-linked tokens (HMT highlights that these share characteristics and risks with unbacked cryptoassets);
3. intends to create a regulated activity under the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (**RAO**) for the issuance of fiat-backed stablecoins in or from the UK. HMT confirms that this will apply to all issuers of fiat-backed stablecoin located within the UK.
4. intends to ensure that the FCA (and, if considered appropriate, BoE) has the power to require that the backing assets of fiat-backed stablecoins are held in a statutory trust. HMT provides that this will enable the FCA and BoE to make rules on requiring the stablecoin issuer (or any other firm safeguarding the backing assets) to hold backing assets for the benefit of customers. The terms of the trust will be set out in the FCA's rules, including when the backing assets

could be paid out of the trust (for example to meet redemption obligations) and how they would be distributed in a firm failure. HMT confirms that the FCA will also consult on these rules prior to their coming into force;

5. intends to create a regulated activity under the RAO for custody comprising the safeguarding, safeguarding and administering, or the arranging of safeguarding or safeguarding and administering of UK issued fiat-backed stablecoins. HMT clarifies that the custody of fiat-backed stablecoins issued outside of the UK will not be captured under RAO; and
6. intends to amend the Payment Services Regulations 2017 (**PSRs**) (which provide for the regulation of authorised or registered payment institutions and set the conditions for providing payment services) to bring into regulation payment chains for:
 - a. mixed stablecoin payments, where the on-ramp to the payment chain is from a stablecoin, but it is converted to fiat within the payment chain, and the off-ramp is in fiat (or vice versa); and
 - b. pure stablecoin payments, where both the on-ramp and off-ramp in the payment chain are in stablecoin and the transfer of value occurs on stablecoin.

The Policy Paper aims to inform the development of the FCA's and BoE's approaches for regulating stablecoin issuers and custodians, and systemic DSA payments systems and service providers respectively. In the next stage of implementation, HMT intends to bring forward secondary legislation "as soon as possible and by early 2024, subject to available parliamentary time".

The BoE's Discussion Paper

The Discussion Paper sets out BoE's proposed regulatory framework for systemic payment systems using stablecoins and related service providers. The Discussion Paper's focus is on Sterling-denominated stablecoin as the BoE considers that these are "most likely to become widely used" for retail payments. In particular, the BoE explains in the Discussion Paper:

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1. how it intends to regulate operators of systemic payment systems using stablecoins and other entities providing services to these payment systems. The Discussion Paper uses stablecoin issuers and wallet providers as an example; and
 2. how it intends to follow a similar regulatory approach as for other payment systems, but will “adapt it appropriately”. The BoE highlights that there will be new regulatory requirements to cover both the risks of stablecoins as a new form of money, and a means of payment.

Comments on the Discussion Paper can be made until 6 February 2024.

The FCA’s DP23/4

DP23/4 sets out the FCA’s proposed regulation around issuing and holding stablecoins that claim to maintain a stable value relative to a fiat currency by holding assets denominated in that currency. Most notably, the FCA proposes to:

1. regulate the issuance and custody of fiat-backed stablecoins under the Financial Services and Markets Act 2000, and the use of these stablecoins as a means of payment under the PSRs;
2. require issuers to always hold backing assets that are: (i) sufficient to back their issued stablecoins; (ii) stable in value; and (iii) sufficiently liquid to support consumers’ right to redeem the regulated stablecoin “promptly”. The FCA further states that backing assets would also need to be properly identified, recorded, segregated, and protected in the event of insolvency of the stablecoin issuer; and
3. apply its rules in the FCA Handbook’s Conduct of Business rules to regulated stablecoin issuers and custodians, restricting the inducements that firms can accept from third parties. The FCA provides that this would cover, for example, commissions and non-monetary benefits.

The FCA has also made it clear that its expectations of firms that provide custody of regulated stablecoins (or the cryptographic “private keys” to access them) would likely be the same when they provide custody of other

types of cryptoassets that come into regulation.

Comments on DP23/4 can be made until 6 February 2024.

The Letter

The Letter sets out how the PRA expects deposit-takers to address risks that arise from issuing multiple forms of digital money to retail customers, with a focus on the risks that may arise in relation to (i) the availability in parallel of deposits; (ii) e-money; and (iii) regulated stablecoins. In addition, the Letter:

1. clarifies the PRA's broader expectations for banks regarding their use of digital money for retail or wholesale innovations, in areas such as operational resilience, anti-money laundering, counter-terrorist financing, and liquidity and funding risks;
2. asks deposit-takers to keep their supervisor updated regarding any material developments in their planned innovations in the use of digital money or money-like instruments, and how their plans meet the expectations set out in the Letter;
3. encourages deposit-takers to read the Letter alongside the Policy Paper, the Discussion Paper, DP23/4 and the Roadmap; and
4. states that the PRA will continue to monitor developments and work with other UK authorities on the development of the overall regulatory framework.

The Roadmap

The Roadmap sets out the Regulators' approach to innovation in payments, money and money-like instruments. In particular, it explains how UK authorities' current and proposed regulatory regimes will interact and clarifies that the Roadmap should be read in conjunction with the Discussion Paper, DP23/4 and Letter. In the Roadmap, the Regulators:

1. explain that they have published their approach jointly to enable them to prevent regulatory arbitrage, provide certainty to firms and developers about the regime applicable to them based on the form of

- money or money-like instrument they want to issue, and maintain the confidence of households and businesses in their ability to make payments on a daily basis;
2. clarify that the frameworks applicable to firms engaged in issuing different forms of money and money-like instruments and operating payment systems will depend on the purpose of their business, how it is conducted, and the risks it presents; and
 3. explain that the BoE and FCA proposals are in an exploratory stage. The BoE and FCA confirm that they expect to consult on more detailed policy proposals and enforceable rules over the course of 2024, with the implementation of such frameworks from 2025.

The Policy Paper, the Discussion Paper, DP23/4, the Letter and the Roadmap are available [here](#), [here](#), [here](#), [here](#) and [here](#) respectively.

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