



Financial Conduct Authority
12 Endeavour Square, London
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10 August 2023

Financial Conduct Authority Guidance Consultation GC23/1: Guidance on cryptoasset financial promotions

Dear Sir or Madam,

Digital Currencies Governance Group (DCGG) and its members welcome the opportunity to comment on the Financial Conduct Authority (FCA)'s Consultation Paper regarding the guidance on cryptoasset promotions.

About Digital Currencies Governance Group (DCGG)

Digital Currencies Governance Group (DCGG) is a trade association that represents digital assets issuers and service providers in the United Kingdom and the European Union. Our mission is to facilitate an open dialogue and encourage communication between policymakers and digital asset experts to support the design of a sound and proportionate regulatory framework that ensures safety for all market participants.

Our Members include Tether - currently the largest stablecoin issuer worldwide, Ledger - a leading technology service provider for self-custody, Bitfinex - a crypto-assets exchange, ZKValidator (ZKV) - a leading proof-of-stake validator, and Iden3 - a solutions provider for self-sovereign identity management.

Overall Position

DCGG supports the implementation of a financial promotions regime for qualifying cryptoassets and commends the FCA for developing guidance for the sector. We believe that expanding this guidance would benefit the overall understanding within the sector of how to promote communications that are compliant. This is especially needed as many firms will be new to this space and an understanding and steer on FCA expectations would be welcomed by industry.

In particular, we would welcome illustrative examples of financial promotions and product categories that will be captured by the regime, how this regime will align with the proposed regulatory framework in HM Treasury's consultation, and how the requirements will balance existing data vs. new requirements for data collections placed on cryptoasset firms. We seek to offer pragmatic views and would welcome the opportunity to discuss any of our points in more detail with the FCA.



Consultation questions

Q1: Do you agree with our proposed guidance on the context of the cryptoasset financial promotions regime? Please explain your answer, highlighting any other issues that would be useful to consider.

DCGG and its members welcome the FCA's initiative in establishing a crypto-specific rulebook for financial promotions. We believe that this is a positive step towards safeguarding and strengthening consumer protection in the cryptoasset market. However, we have identified several potential issues that we would like to highlight to inform this consultation's findings.

Issue 1: Applicability to the online presence of cryptoasset service providers

We agree with the FCA that risk warnings should be displayed in a clear and prominent manner across different mediums of communication. However, there is a degree of ambiguity in the interpretation of what amounts to an 'invitation or inducement' to engage in investment activity that is communicated in the course of business.

This is acknowledged by the FCA in PERG 8.4 with further acknowledgment that promotional communications only are intended to be captured. This is distinguished from communications that seek to inform or educate without an element of persuasion. However, DCGG believes that there is still ambiguity that remains in interpreting whether materials on a website seek to inform or persuade a consumer to invest. This can result in market uncertainty regarding the requirements facing cryptoasset businesses under the financial promotions regime.

As an example, a cryptoasset exchange may display purely factual information with no invitation or inducement to invest other than a 'buy' button displayed at the top of the website. An interpretation that this would amount to a financial promotion, and a subsequent requirement for authorisation, would, in DCGG's opinion, be too onerous a requirement that does not take into account reverse solicitation and the rationale behind consumers actively seeking out the website, or controlled activity. We recognise this example cannot be without nuance, such as the consumer's journey to arrive at the website. However, we view a prescriptive approach that would capture the presence of such a button as an inducement that would require a financial promotion approval to act as a strong deterrent to offering such services in the UK, which would damage consumer choice as well as overall reputation and competitiveness.

Issue 2: Efficiency of the new rules

We are concerned that some of the new rules could be seen as highly inefficient by UK and non-UK cryptoasset issuers and providers alike, and in certain cases, unrealistic for most businesses to rely on. Specifically, we are concerned that there



will be a lack of approved firms with the necessary competence and expertise to approve cryptoasset firms, or are otherwise discensitised from doing so for competitive reasons. Further to this point, adding an approval element to output through social media may make the use of such channels impractical.

Additionally, we believe the AML requirements will still be considered onerous for firms that do not plan to undertake a significant investment in the UK market, and the potential delay in applications being processed. Indeed, a large part of the impact of the financial promotions regime is in the way it applies to overseas cryptoasset firms. However, previous FCA guidance in relation to the process for approval under this route appears - at least in intent - only to apply to firms who are carrying on business in the UK, ultimately driven by whether the firm has a UK office or other activity (beyond having clients in the UK). For many firms operating without carrying on business in the UK, the prospect of registering under the MLRs purely to manage the risks arising from the financial promotions regime is not practical.

In order to overcome some of these issues, we would welcome specific consideration to 'fast tracking' s21 approvers and reducing the costs and requirements for prospective applicants under the proposed gateway. We would also welcome further guidance on when this gateway will apply in order to support cryptoasset businesses seeking compliance for financial promotions that are capable of having an effect in the UK. We believe there is a significant risk of firms geoblocking services to the UK, which will undermine the UK's commitment to becoming a global hub for crypto investment and technology and improve the UK's medium to long-term growth.

Issue 3: Complexity of the new rules for international firms

Given that the updated rulebook intends to capture the promotions of domestic and international issuers and providers, we expect that the process will be highly complex to navigate for international firms. We urge the FCA to provide further clarity as to how it will work with domestic and international firms, especially during the initial period post-enforcement, rather than seeking to implement consequences such as bans or fines.

The guidance does not currently specify the territorial scope of the financial promotions regime. The FCA has provided general guidance on this topic in PERG 8.3, but this does not address the specific concerns of cryptoasset businesses. As stated above, the new rules will impact cryptoasset businesses for the first time. Many of these businesses offer services into the UK on a cross-border basis. As a result, there is a need for specific guidance on the territorial scope of the financial promotions regime for cryptoassets.

Recommendation: Financial promotion rules related to online websites should take into account reverse solicitation. Further consideration should also be given in accordance to how the new s.21 gateway will work in practice for cryptoasset firms.



Q2: Do you agree with our proposed guidance on ensuring that cryptoasset financial promotions are fair, clear and not misleading? Please explain your answer, highlighting any other issues that would be useful to consider.

DCGG supports 'fair, clear, and misleading' rules across all financial promotions. However, we strongly urge the FCA to enhance its guidance and support the industry's understanding by providing illustrative examples that effectively demonstrate both positive and negative promotion practices. Drawing inspiration from the regulator's comprehensive non-Handbook guidance, such as the Consumer Duty rules, we propose that the FCA incorporate case-specific scenarios tailored to the intricacies of the cryptoasset industry, taking into account aspects like decentralisation, blockchain technology, and mining.

We also believe that there is a significant burden that will be placed on cryptoasset firms in relation to comprehensive risk disclosures. This appears to deviate from the guiding principle of presenting a "balanced view" and contravenes the established proportionality that generally governs the realm of financial promotions. As a result, we believe the industry would benefit from supplementary guidance on this specific issue, including a clearer delineation of expectations.

Q3: Do you agree with our proposed guidance for financial promotions of cryptoassets that claim a form of stability, or which claim their value is linked to a fiat currency? Please explain your answer, highlighting any other issues that would be useful to consider.

DCGG and its members have identified some concerns in relation to reserves requirements and treatment in the proposed guidance for financial promotions of cryptoassets that claim a form of stability or claim their value is linked to fiat currency.

We are concerned with the rationale put forward in PS23/6 regarding the communication of value linked to the value of a fiat currency. In particular, firms would be required to demonstrate that claims of stability or links to a fiat currency are "**bona fide**".

It is very common for issuers of fiat-denominated stablecoins to implement cash and cash equivalents and other forms of highly liquid and secure assets to diversify their reserves pool (e.g., government bonds), which also leads to higher levels of security, whereby the cryptoasset's stability does not rely on solely one type of underlying asset and any concentrated counterparty risk is reduced.

As such, we encourage that cash equivalents and other forms of highly liquid assets are included in the definition of "bona fide" in this context, which may require promotions to clearly disclose the underlying reserves pool to consumers.



In general, we view the requirement for disclosure to require a degree of proportionality. The right level of disclosure is difficult to achieve, however we remain concerned that more disclosure does not necessitate better customer outcomes and make it harder for customers to assess the product. Furthermore, firms will need to rely on third party issuers for this information, which is practically difficult and expensive. As such, we believe using existing available information on how stablecoins maintain their stability would be the most practical and proportionate approach. Overall, we believe this will also create market incentives for firms to improve their data which is shared with consumers.

Additionally, we do not encourage the application of a "**one-size fits all**" approach regarding the promotions obligations of different types of stablecoins. Fiat-denominated stablecoins have historically demonstrated more resilient stability mechanisms than the ones of algorithmic and crypto-backed stablecoins, as evidenced in the FCA's rationale outlined in the guidance document. The underlying stability mechanism directly affects the levels of risk associated with the asset, and we believe separate guidance for promotions disclosures should be enforced for these types of assets (i.e., with algorithmic or crypto backing), in order to adequately reflect the higher risk levels.

Q4: Do you agree with our proposed guidance for financial promotions of cryptoassets that claim to be backed by a commodity or an asset? Please explain your answer, highlighting any other issues that would be useful to consider.

DCGG supports transparent disclosures regarding the ownership and conditions for investing and holding commodity-linked cryptoassets, as customer interest in such assets continues to grow. We agree with the majority of the proposed guidance, however we would like to highlight two areas of concern that should be taken into account ahead of enforcing the updated financial promotions framework.

Firstly, the guidance set out in this consultation provides little clarity as to whether the underlying commodities of such cryptoassets (e.g., gold), should only be held/custodied on UK territory to allow issuers to promote to UK citizens. From our perspective, the location of the underlying commodity should not be a factor for consideration of risk assessment, as long as the location, transport costs, redemption conditions and other related fees or potential associated risks are clearly disclosed in promotional communications required for operators to comply with the FCA's guidance.

Secondly, to ensure the proposed regulatory approach is fair and balanced and does not place excessive administrative burden of certain actors only (in this case, commodity-linked cryptoassets), we suggest that the FCA aligns the provisions under paragraph 52 of this guidance consultation on complex yield models (i.e., risk



assessment to be based on publicly available evidence), with the guidance for promotions of commodity-linked tokens.

In particular, the proposed assessment for proof of ownership, such as independent audits and proof of deposits, should be made based on publicly available evidence put forward by the issuer, as these are conducted on a regular basis and are the current industry standard practice in the case of regular assurance on reserve reports (sometimes referred to as “attestations”), and should be sufficient data for conducting a risk assessment regarding proof of ownership of the commodity-linked cryptoasset.

We discourage requiring issuers to conduct separate audits for the purposes of promotions, as depending on the underlying commodity and operational structure of the token, this could be very costly and burdensome for the issuer to do outside of its established timeframe for auditing, and holds issuers to a unnecessarily high financial standard. Furthermore, such requirements under the financial promotions rules would be considered amounting to a regulatory regime for cryptoassets, which we understand will be consulted on in due course.

Q5: Do you agree with our proposed guidance for financial promotions of complex yield models or arrangements? Please explain your answer, highlighting any other issues that would be useful to consider.

DCGG agrees with the conditions that are required to be met by providers of complex yield models/arrangements for the purposes of communicating financial promotions, including standards around promoting return rates. However, we would like to emphasise that certain assets that are part of such arrangements can experience higher levels of volatility than others, which could affect the rates of return.

Importantly, investors should be empowered to partake in such activities in alignment with their risk appetite. Therefore, we encourage the FCA to clearly set out that, as long as complex yield arrangements providers clearly (and in accordance with the proposed guideline) disclose to customers through communication of promotions that specific risks are involved and that levels of volatility can sometimes vary despite the initially predicted rates of return, promotions should not be considered ‘misleading’ and liability for being classified as not clear or fair, or misleading, should not sit with these providers if rates are affected by asset volatility outside of their control.

Q7: Do you agree with our proposed guidance on due diligence before a financial promotion is communicated? Please explain your answer, highlighting any other issues that would be useful to consider.

Regarding the due diligence guidance prior to the communication of financial promotions, DCGG and its members wish to express our reservations concerning the proposed consideration of "ensuring the cryptoasset is not linked to fraudulent activity,



scams, money laundering or other financial crime". We are concerned that this proposed consideration, once implemented, could potentially give rise to challenges, as its breadth potentially places an excessive burden on the promoter of the communication.

It is our view that an investigation of every possible link of a cryptoasset to these activities will carry a significant administrative burden for firms - or otherwise be an impossible task. Additionally, this requirement may disproportionately limit promotions related to widely used cryptoassets, where illicit activities are more likely to occur.

We recognise and support the FCA's acknowledgement that there is not a 'one-size fits all approach' and that firms should take a pragmatic approach. We believe this principle could be better reflected in the guidance to provide more certainty to businesses. In particular, to address the potential adverse implications and mitigate the impact of this proposal, we believe the guidance should focus on firms placing risk warnings with the promotion to inform the customer of the possibility of such instances of illicit activity occurring. This, in our opinion, would achieve the objective of ensuring the promotion is fair, clear, and not misleading, without placing significant administrative burdens on firms, or risking an outcome where less established cryptoassets (and therefore more risky) are perceived as more favourable forms of promotions.

Should the FCA decide to continue with this requirement, we believe consideration could be given to avoiding duplication and administrative costs facing firms in conducting such due diligence. In this respect, DCGG would support an FCA-approved list of cryptoassets that could be relied upon as having gone through sufficient and approved due diligence. This would provide confidence to firm's in communicating a promotion, and remove time and cost-sensitive requirements as outlined in the guidance in its current form. Should a cryptoasset not be on this list, for a variety of reasons, then due diligence conducted by the promoter could support an FCA assessment of whether to add the cryptoasset to the list.

Overall, we believe that adding a risk warning that there is potential for a cryptoasset to be linked to illicit activity will be sufficient for improving consumer awareness and safety. Furthermore, we also understand that the guidance appears to share some similarities with the proposals outlined in HM Treasury's consultation on the future regulatory treatment of cryptoassets. While we understand that detailed principles will be defined by the FCA in any future rulebook, we believe there is a risk that the guidance related to financial promotions will 'frontrun' this work and may result in divergent regulatory regimes, or create uncertainty in the market.

To mitigate the aforementioned risks, we recommend the FCA takes a phased approach to this section of the guidance. Specifically, to initially introduce a lighter-touch due diligence framework that requires cryptoasset platforms to clearly disclose



risks (rather than a requirement to attest to issuers' technological and operational capabilities) until broader, overarching legislation is enforced to govern these matters, at which point issuers would be required to provide this information to the market. This way operators would not be required to comply with such a short timeframe and the onus would be reduced until future legislation has entered into force and rules are harmonised.

We would also welcome clarity from the FCA that the extension of the financial promotions regime's obligations will not encompass the listing of tokens on exchange websites, and how the relevant due diligence requirements will relate to the proposal approach in HM Treasury's consultation. We would welcome explicit guidance on these issues, as well as information on the assessment of ESG credentials and technological qualifications given the lack of established procedures or precedent. Practical examples that demonstrate where and how these due diligence standards should be applied would be particularly welcomed.

Q10: Are there any other topics you believe our guidance should cover?

DCGG and its members welcome the guidance consultation document on financial promotions for cryptoassets.

We would welcome further clarity on the perimeters for a financial promotion to have an 'element of persuasion'. For example, we understand that a promotion of a non-custodial wallet would not be captured as a financial promotion or controlled activity given it does not fit within the definition of a qualifying cryptoasset. However, we understand that should a promotion include details related to a captured or controlled activity it could be considered a financial promotion under the new rules and therefore require approval.

However, it is not clear whether such a promotion that references a qualifying cryptoasset would necessarily be captured if it seeks to 'invite' or 'induce' the viewer of the promotion into purchasing an activity that is not a qualifying cryptoasset, such as the non-custodial wallet using the example above (e.g., 'our wallet offers the best method of looking after your bitcoin. Buy now!'). Clarity over whether this would be captured, or the extent of the reference to the qualifying cryptoasset would bring it within scope, would be welcomed by the industry.

Discussion questions on complex yield models/arrangements

Q1: What are the benefits and opportunities of cryptoasset borrowing, lending and staking models/arrangements for consumers?



The confluence of unmet financial needs and innovative technology, exemplified by self-executing smart contracts, creates a secure and pioneering financing avenue for lenders and borrowers alike, fostering certainty and accessibility. This creates several opportunities:

- **Enhanced Financial Inclusion:** Innovative technologies can democratise financial services through new products and services, bridging gaps for underserved segments.
- **Swift, Transparent, Immutable Transactions:** Underlying technology reinforces transactions' efficiency and transparency, bolstered by robust security protocols.
- **Diversification of Investment Portfolio:** Crypto lending, borrowing, and staking afford diversification avenues for investors.
- **Liquidity Access:** Participants benefit from readily available liquidity.

The dynamic landscape facilitated by these practices not only advances financial inclusion but also underpins rapid, traceable, and immutable transactions, fortified by robust security. The interplay of these components advocates for consumer well-being, while concurrently nurturing an environment conducive to economic growth in the UK's pursuit of becoming a crypto hub.

Q2: Which type of cryptoasset borrowing, lending and staking models/arrangements provide the greatest benefit to consumers?

DCGG believes that cryptoasset lending and staking activities requires further granular definitions:

'Staking'

- **Liquidity Provision Staking and DeFi Locking:** The utilisation of tokens post-locking diverges from staking for network security. Tokens engaged in DeFi may be interpreted as lent assets, adding value to a liquidity pool. Liquidity pools are collections of digital funds locked in a smart contract. This offers greater potential rewards for users, but also comes with higher risk as it may result in financial loss.
- **Staking for Blockchain Network Security:** Staking, employed to ensure blockchain network robustness, embodies a critical validation procedure, culminating in heightened security and consumer well-being. This variant of staking boasts relative stability with transparent and rigorously defined risks, clearly delineated within the network's code and documentation. As such, this form of staking can be considered more akin to a savings account.

'Lending'



- **Cryptoasset Lending:** Lending and borrowing constitute a substantial portion of operations within the cryptoasset and DeFi sector. Specialised lending platforms present a diverse range of business frameworks, some of which bear resemblances to conventional practices, including collateralised lending, peer-to-peer lending, securities lending (as exemplified by exchanges offering margin loans), investment management, and unsecured credit offerings.

While staking for blockchain network security is characterised by low risk, the act of staking for DeFi liquidity echoes lending's traits, presenting comparatively elevated risk levels similar to traditional lending, where the borrower's potential incapability to repay the loan poses an enhanced risk to their cryptoassets and financial security.

However, DCGG believes that all cryptoasset borrowing, lending, and staking models/arrangements can provide benefits to consumers, but that the benefits and risks of each model vary in accordance with consumers' risk appetites, which may be driven by the activity which they choose to engage in, or the type and security of the collateralised asset that is 'lent out'.

Q3: What are the risks associated with cryptoasset borrowing, lending and staking models/arrangements for consumers?

Cryptoasset borrowing and lending: Cryptoasset borrowing and lending are bank-like activities that carry their distinct level of risk. Specifically, engaging in bank-like activities without liquidity requirements, or additional safeguards such as a minimum loan over collateralisation threshold, government support, or deposit insurance, creates an environment of heightened risk for consumers to face potential losses when 'runs' on platforms occur.

This can lead to a scenario where depositors rush to withdraw funds, forcing lending platforms to sell assets at distressed prices to meet redemptions. Such fire-sale dynamics can also cause contagion, affecting other market participants in a similar position, either through direct exposure or through creating volatility for collateralised assets underpinning the borrower/lender relationship.

In particular, lending (where transfer of the asset is transferred) is a more traditional financial activity that carries with it a greater risk of loss for consumers. In lending, the borrower is typically taking on debt and may not be able to repay the loan which could result in the loss of the borrower's cryptoassets.

In this scenario, the level of consumer protection that is appropriate for each activity may vary depending on the specific circumstances, including value and the nature of the asset which is lent. It is important to consider the volatility of the collateralised asset, with stablecoins for example offering better security and less risk of volatility for consumer's assets. Furthermore, improving customers' understanding of the risk,



while heightening the presence of publicly-available risk and lending information (e.g., ratings) that will support the development of a transparent and ultimately more secure cryptoasset lending and borrowing activities, is important.

Cryptoasset staking: As mentioned above, staking in the context of DeFi liquidity provision is deemed to carry higher risk to consumers. It is important that future oversight takes these differences into account. We believe that staking for DeFi liquidity provision is more akin to a lending activity with higher levels of risk and informing consumers of the risks and preventing misuse of how staking is promoted would be critical. However, the decentralised nature of this activity makes it challenging to regulate at this stage from both a promotions and general regulatory perspective.

Q7: Are there any other issues we should take account of when considering our approach when developing regulatory requirements for cryptoasset borrowing, lending and staking models/arrangements?

Related to financial promotions, we share similar concerns to some of the respondents regarding the 24-hour cooling-off period proposed in CP 22/2 that the value of cryptoassets may vary during this timeframe. Further clarity would be welcomed regarding the way the potential FCA guidance on complex yield arrangements would take volatility into consideration and what stage of the consumer journey would be captured under the remit of promotions regulations in order to facilitate compliance for providers.

Furthermore, we anticipate that prudential or reserve requirements will be addressed in the future rules related to the regulatory regime for cryptoassets. We believe that the FCA should avoid using the financial promotions regime as the mechanism for implementing additional regulatory requirements (e.g., prudential requirements / capital ratios etc) given the main aim of the financial promotions regime is to improve consumers' understanding of the current risks involved investing in a controlled activity.