

# The Distributed Ledger

## Blockchain, Digital Assets and Smart Contracts

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One Manhattan West  
New York, NY 10001  
212.735.3000

22 Bishopsgate  
London EC2N 4BQ, UK  
44.20.7519.7000

### Cryptoassets Will Soon Be Subject to UK's 'Financial Promotions' Regulations

On 7 June 2023, the UK Parliament passed the Financial Services and Markets Act 2000 (Financial Promotion) (Amendment) Order 2023, which brings cryptoassets within the scope of rules that regulate the marketing of financial products in the UK. The statutory instrument amends the Financial Services and Markets Act (Financial Promotion) Order 2005 (FPO), extending it to cryptoassets with effect from 8 October 2023. The FPO defines the investments and activities captured by the financial promotions regime as well as related exemptions.

On 8 June 2023, the Financial Conduct Authority (FCA) published a policy statement setting out the final rules on cryptoassets promotions (PS 23/6). The formal inclusion of cryptoassets within the financial promotions regime is taking place against the backdrop of the UK government's strategy to ensure that the UK is a hub for cryptoassets while balancing that goal with adequate consumer protections.

### The Financial Promotions Restriction

Section 21 of the Financial Services and Markets Act 2000 (FSMA) sets out the restrictions on the making of "financial promotions" (Financial Promotions Restriction) in the UK. Broadly, this restricts firms from undertaking marketing and communications in relation to investment activities unless:

- the relevant firm is authorised by the FCA (an authorised person);
- the relevant communication has been approved by an authorised person; or
- the relevant marketing or communications activity falls within an exemption to the FPO.

A "financial promotion" is any invitation or inducement to engage in investment activity, which includes dealing in, arranging deals in or advising on deals relating to certain investments (which will include cryptoassets). Promotions made on websites, apps, social media and online advertising qualify, as well as, for example, posters and advertisements on public transport. Financial promotions should be "stand-alone compliant," meaning that each stage of a communication is subject to the rules.

This is particularly significant where advertisements contain hyperlinks and separate pathways to further information about cryptoassets.

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### Amendments to the Financial Promotions Order To Include Cryptoassets

Under PS 23/6, a “qualifying cryptoasset” will now be included as a type of investment covered by the FPO.

A “cryptoasset” is defined as:

any cryptographically secured digital representation of value or contractual rights that (a) can be transferred, stored or traded electronically, and (b) uses technology supporting the recording or storage of data (which may include distributed ledger technology).

A “qualifying cryptoasset” is one that is fungible and transferrable. While excluding electronic money and certain cryptoassets that may only be used in a limited way,<sup>1</sup> such as NFTs, NFTs could be a qualifying cryptocurrency if (i) they have features such as fractionalisation that would cause them to become fungible or (ii) they are otherwise regarded as a type of financial product covered by the FPO.

Importantly, the amendments to the FPO provide additional ways for firms to comply with the Financial Promotions Restriction, for example, by permitting cryptoasset firms that are not UK-authorized but are merely registered with the FCA for anti-money laundering purposes<sup>2</sup> to issue financial promotions or approve financial promotions made by other unauthorised or non-registered cryptoasset firms. Without this dispensation, FCA-registered firms would have to either seek authorisation or obtain approval of their financial promotions from an authorised person.

In practice, this new rule may not make much difference, because cryptoasset firms would not typically require FCA authorisation, and existing FCA-authorized firms may be reluctant to approve the financial promotions of other cryptoasset firms given that they would need to adopt some degree of responsibility for the content of such promotions.

In addition, obstacles will likely remain, because many cryptoasset firms are not succeeding in their applications for FCA registration at present. Currently, there isn't a sizable number of FCA-registered cryptoasset firms, and fewer still that would be willing to provide approvals of the financial promotions of other firms.

If firms that are within the scope of the Financial Promotions Restriction are unable to obtain FCA registration or have their

<sup>1</sup> These conditions being it allows the holder to acquire goods or services only from the issuer; it is issued by a professional issuer and allows the holder to acquire goods or services only within a limited network of service providers that have direct commercial agreements with the issuer; or it may be used only to acquire a very limited range of goods or services.

<sup>2</sup> As set out in Regulation 57 of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulation 2017.

promotions approved, they will need to curtail their promotions either by avoiding making them in the UK or by ensuring that promotions only go to recipients that fall within exemptions. The FPO includes a number of exemptions typically used by unauthorised firms (including non-UK firms seeking to market to UK customers), which may be useful for crypto firms. These exemptions cover financial promotions with respect to:

- Financial institutions (Article 19 FPO).
- Entities above certain size thresholds (Article 49 FPO).
- Certain high-net-worth individuals (Article 48 FPO).
- Certain sophisticated investors (Articles 50, 50A FPO).

### Near-Final FCA Rules for Financial Promotions

Following an FCA consultation in January 2022, the FCA simplified its financial promotions rules by arranging the rules according to three product categories:

1. Readily Realisable Securities, which are not subject to any marketing restrictions.
2. Restricted Mass Market Investments (RMMIs), which are subject to certain restrictions.
3. Non-Mass Market Investments, which may not be marketed to retail investors.

The FCA's Policy Statement classifies cryptoassets as RMMIs. This means that financial promotions will need to comply with a number of rules set out in the FCA Handbook, in addition to the overarching requirement that the promotions must be fair, clear and not misleading. The requirements include the following:

- Promotions must include a risk warning and an associated risk summary.
- Monetary and non-monetary incentives to invest are prohibited.
- Directive Offer Financial Promotions<sup>3</sup> (DOFPs) including consumer journey protection are subject to additional rules.
- New investors shall be afforded a 24-hour cooling-off period.
- Client categorisation.
- Appropriateness assessments must be performed prior to showing a customer any DOFPs, *i.e.*, the recipient's knowledge and experience in relation to the risks associated with the cryptoasset must be evaluated.

<sup>3</sup> DOFPs are defined in the FCA Handbook as a financial promotion that contains: (a) an offer by the firm or another person to enter into a controlled agreement with any person who responds to the communication; or (b) an invitation to any person who responds to the communication to make an offer to the firm or another person to enter into a controlled agreement; in either case specifying the manner of response, or including a form by which a response may be made. For example, making an offer on a leaflet with a tear-off slip.

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- Record-keeping requirements must be adhered to.
  - Date- and time-stamping requirements for authorised firms approving financial promotions.

### Next Steps for Firms

The new rules will come into effect on 8 October 2023. Firms operating in the cryptoasset space and currently seeking FCA registration will need to consider compliance with the new

Financial Promotions Restriction. Unauthorised firms, including those based outside the UK, will need to consider their marketing efforts in the UK in respect of cryptoassets and how they can comply with the Financial Promotions Restriction. In addition, the FCA is consulting the industry with a view to drafting further guidance on how firms can comply with the general requirement that financial promotions for cryptoassets must be fair, clear and not misleading.

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## Contacts

### Simon Toms

Partner / London  
44.20.7519.7085  
simon.toms@skadden.com

### Danny Tricot

Partner / London  
44.20.7519.7071  
danny.tricot@skadden.com

### Azad Ali

Of Counsel / London  
44.20.7519.7034  
azad.ali@skadden.com

### Adam M. Howard

Counsel / London  
44.20.7519.7091  
adam.howard@skadden.com

### Justin Lau

Associate / London  
44.20.7519.7029  
justin.lau@skadden.com

### Olivia Moul

Trainee Solicitor / London  
44.20.7519.7636  
olivia.moul@skadden.com

### David Y. Wang

Associate / London  
44.20.7519.7149  
david.y.wang@skadden.com