

The Distributed Ledger

Blockchain, Digital Assets and Smart Contracts

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UK Cryptoasset Financial Promotions: FCA Takes Firm Stance on Enforcing New Rules

The landscape of cryptoasset regulation in the UK entered a new phase in October 2023 with the extension to cryptoassets of marketing restrictions for financial products and services. In particular, crypto firms based outside the UK and marketing in a way that is capable of having an effect in the UK must now consider whether their website and other communications are in scope of the UK rules. In certain cases such firms must (a) seek out a firm authorised with the Financial Conduct Authority (FCA) or the Prudential Regulatory Authority to approve their communications or (b) geo-block UK users.

Many firms and market participants have been surprised at the breadth of the restrictions and the FCA's rigorous day-one approach to enforcement, although the FCA's early warnings before the regime came into force signalled the strict approach it would take. That contrasts with the government's firm ambition for the UK to embrace the crypto industry. A government minister has reportedly written to the FCA requesting the FCA exercise forbearance in applying the new rules and has urged the FCA to promptly issue finalised guidance to the crypto industry.

It will be interesting to see how this tension between the government and the FCA plays out.

Background to the Financial Promotions Restriction

The financial promotions restriction has broad application. The restriction is not limited to just active marketing or targeting of customers by firms. It captures any (i) "communication" which has an element of (ii) an "invitation or inducement" to (iii) "engage in investment activity".

- Website and other communications (e.g., through social media) would count as "communications" and may well amount to an "invitation or inducement".
- "Inducement", in particular, is broadly defined, and the FCA states that this will capture any significant step in a chain where the chain is intended to lead to an agreement to "engage in investment activity".
- Frequently, the element of "engaging in investment activity" — including dealing in, arranging deals, advising on or managing cryptoassets — is key to answering whether the crypto firms fall into scope.

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To fall within the new regime, the financial promotion must also relate to a “qualifying cryptoasset”, which is broadly defined. There are limited exceptions for certain tokens that are deemed non-fungible or non-transferable, or are otherwise limited in their use.

The FCA Adopts Strict Position on Compliance

Prior to the introduction of the new rules, the FCA warned firms that it expected them to do more to comply with the regime, and within 24 hours of the rules taking effect, it announced that it had written to 146 firms regarding non-compliance, and included them on the FCA’s Warning List of “unauthorised firms”. This suggests it had been actively monitoring the position of firms in the run-up to the introductions of the new rules.

The extensive reach of the financial promotions restriction, coupled with the FCA’s strong focus on compliance, has forced firms to consider the size of the UK market for their business, even if the UK is not actively targeted as a market for their cryptoassets.

What Should Firms Do Now?

There are few easy options available. Aside from geo-blocking UK users, crypto firms could (i) perform a review of all communications available to UK users for promotional language; (ii) enter into arrangements with a UK-authorized firm for cryptoasset promotions to be approved or (iii) seek registration under the UK’s anti-money laundering regime for cryptoasset firms, because such firms are exempt from the financial promotions perimeter (although they are unable to approve promotions in a manner similar to an authorised person).

Seeking a financial promotions approver. It is important to note that there are few firms that are willing to approve third-party financial promotions (an Approving Firm), and a regime recently came into place requiring Approving Firms to seek additional FCA authorisation to act in that role.

The process for approval will not be simple because there are a number of steps that cryptoasset firms will need to go through. The Approving Firm will need to conduct due diligence on the cryptoasset firm to make sure that the Approving Firm has the expertise regarding the cryptoassets encompassed by the promotions that it is approving. The cryptoasset firm will also need to put in place risk warnings, perform appropriateness assessments and categorise clients. See our 21 June 2023 client alert “Cryptoassets Will Soon Be Subject to UK’s ‘Financial Promotions’ Regulations”.

Seeking UK-authorisation or registration. There is currently no authorisation regime in place in the UK for regulated activities relating to cryptoassets. Therefore, a cryptoasset firm that seeks authorisation would need to apply for permissions relating to activities and services that they may not actually perform — for example, applying under the Markets in Financial Instruments Directive (MiFID) regime for investment firms or the payment services regime. See our 2 February 2023 client alert “New Consultation on UK Cryptoasset Regulation: Amid Market Turbulence, Government Pursues Plans To Become a Global Crypto Hub”.

Registration may similarly be unfeasible if a firm does not have a UK presence. One of the elements of the UK anti-money laundering perimeter is that a firm cannot obtain UK registration without a UK office. The FCA has said it expects a money laundering reporting officer (MLRO) to be based in the UK. Moreover, money laundering registrations can take up to 12-18 months or longer, and have been heavily scrutinized by the FCA. In the last 12 months, only 6% of all applications have led to a successful registration.

In sum, cryptoasset firms should be aware that the FCA will continue to vigorously enforce the new rules and they should therefore tread lightly in navigating them.