



HM Treasury

Cryptoasset promotions: Consultation response

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Chapter 1

Introduction

Background

- 1.1 In July 2020 the government published a consultation (hereafter ‘the consultation’) on a proposal to bring certain cryptoassets into the scope of the Financial Promotion Order (the ‘FPO’).¹ This document outlines the government’s response and summarises feedback received.
- 1.2 The Cryptoassets Taskforce, consisting of HM Treasury, the Bank of England and the Financial Conduct Authority (‘FCA’) published a report in 2018, which found that misleading advertising and a lack of suitable information was a key consumer protection issue in cryptoasset markets. ² The report found that cryptoasset advertising, which is often targeted at retail investors, can often overstate benefits and rarely warns of volatility risks. This includes the risk that consumers can both grow and lose their investment.
- 1.3 Since the report, the cryptoassets market has continued to evolve. Recent findings from the FCA suggest that ownership has risen, while the level of understanding of cryptoassets appears to be declining, suggesting that some holders may not fully understand the risks involved.³ The government believes that these findings further support the case for regulatory intervention to ensure that cryptoasset promotions are fair, clear, and not misleading. Further details on the FCA’s market research can be found on the FCA’s website.
- 1.4 The government has adopted a staged and proportionate approach to cryptoassets regulation, which is sensitive to risks posed, and responsive to new developments in the market. This measure, to expand the scope of the Financial Promotion Order to capture certain cryptoassets, complements broader proposals on cryptoassets and stablecoins set out via the government’s consultation on a regulatory framework for stablecoins earlier this year. It also aligns with separate government proposals to strengthen the authorisation process for financial promotions.
- 1.5 This document outlines how the government will ensure appropriate regulation of cryptoasset promotions, where the government has identified potential risks to consumers. The government will continue to assess new

¹ Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (SI 2005/1529)

² The Payments Systems Regulator (PSR) joined the Cryptoassets Taskforce in 2020.

³ <https://www.fca.org.uk/publications/research/research-note-cryptoasset-consumer-research-2021>

and emerging risks from cryptoassets as this market continues to mature and will take further action if required.

- 1.6 The government has carefully considered the responses to the consultation. The government is grateful to the 25 respondents to the consultation, including firms, trade bodies, and committees and members of the public. The government held a roundtable with industry stakeholders during the consultation period and held meetings with trade associations to discuss key issues raised in consultation responses.

The structure of this document

- 1.7 The structure of this document is as follows:
- an overview of the Financial Promotion Order
 - a summary of the government's approach to cryptoasset financial promotions
 - a summary of the regulatory scope for cryptoasset financial promotions
 - annex A: summary of responses received to the consultation

Chapter 2

Overview of the Financial Promotion Order

- 2.1 Responses to the consultation agreed that misleading advertising and a lack of suitable information means there are consumer risks present in the cryptoassets market, and there was broad agreement on the case for intervention.
- 2.2 The government will therefore act to ensure the appropriate regulation of cryptoasset promotions through secondary legislation, broadly in line with the proposals set out in the consultation.
- 2.3 This chapter sets out how the Financial Promotion Order operates.
- 2.4 Financial promotions play an important role in the financial decisions made by individuals. Consumers are influenced by the substance and presentation of promotions, which can have a significant impact on whether they decide to engage with a particular financial service provider or use a particular financial product.
- 2.5 The communication of financial promotions is subject to regulatory safeguards which seek to ensure that consumers are appropriately protected such that they are able to make informed and appropriate decisions. The UK financial promotion regime provides safeguards in two key ways:
- in general, an individual or business cannot communicate a financial promotion unless either the content of the promotion is approved by a firm which is authorised by the FCA or Prudential Regulation Authority to carry on a regulated financial services activity, or the individual or business holds such an authorisation itself; this is referred to as the ‘financial promotion restriction’
 - the FCA sets binding rules that authorised firms must comply with when communicating or approving financial promotions, for example, the requirement that financial promotions must be fair, clear and not misleading; this is a requirement is set out in the FCA’s rulebook, in the Conduct of Business Sourcebook (COBS) 4¹
- 2.6 Section 21 of the Financial Services and Markets Act 2000 (‘FSMA’) contains the financial promotion restriction. This restriction is broad in scope and provides that a person must not, in the course of business, communicate an invitation or inducement to engage in investment activity or claims management activity. This includes invitations or inducements to engage in certain activities which are not regulated activities. For example, a person

¹ <https://www.handbook.fca.org.uk/handbook/COBS/4/?view=chapter>

may not necessarily be carrying on a regulated activity requiring authorisation when issuing bonds, but the marketing of the bonds is likely to be subject to the financial promotion restriction. The financial promotion restriction does not apply if:

- the communication is made by an authorised person;
- the content of the communication is approved by an authorised person; or
- the financial promotion otherwise meets the conditions of an exemption within the Financial Services and Markets Act 2000 ('FSMA') (Financial Promotion) Order 2005 (FPO)

2.7 The Financial Promotion Order sets out a list of controlled investments that are captured by the legislation, and controlled activities that apply to these investments. The promotion of engaging in investment activity is restricted under the Financial Promotion Order, which relates to agreements constituting a controlled activity, or exercising any rights conferred by a controlled investment. Controlled investments under the Financial Promotion Order currently include, for example, government and public securities, options and futures. The list of controlled activities includes, for example, dealing in securities and contractually based investments, arranging deals in investments, and managing investments.

2.8 The government is also making changes to introduce a new regulatory gateway for firms approving financial promotions for unauthorised firms (known as the 'section 21 gateway'). This proposal involves amending FSMA to impose a new requirement on authorised firms, requiring that they will only be able approve financial promotions for unauthorised persons if they have been assessed by the FCA as suitable to do so. Further information on the government's proposals and response to the consultation can be found on GOV.UK.²

2.9 Communicating a financial promotion in breach of section 21 is a criminal offence on the part of the unauthorised person under section 25 of FSMA. If the FCA finds that a financial promotion which is communicated or approved by an authorised firm breaches its rules, the FCA will usually engage with the authorised firm to request that the promotion is changed or withdrawn. If the FCA is not satisfied with the response of the authorised firm, it has a broad power to direct the firm to address the breach which may include directing the firm to withdraw its approval of the promotion. The FCA can also open an investigation which can lead to enforcement action (such as a financial penalty) if serious misconduct is discovered.

2.10 The FCA's Handbook contains rules on financial promotions which authorised persons must comply with when communicating or approving financial promotions. These rules include the basic requirement that financial promotions must be 'fair, clear and not misleading'. Authorised firms, whether communicating their own financial promotions or approving the

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https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/995565/HMT_WR_113_Consultation_Response.pdf

promotions of unauthorised firms, are obliged to ensure that promotions are compliant with these rules. The FCA rules do not generally apply to financial promotions where an exemption applies.

- 2.11 In addition, the FCA has used its financial promotions rule making power over recent years to impose marketing restrictions which limit the extent to which firms can promote investments which the FCA has classified as high-risk to retail investors. For example, speculative mini-bonds cannot be marketed to retail investors (unless they are high net worth or sophisticated). In recent years the FCA's marketing restrictions have taken on an increasingly significant role as structural changes in the retail investment market mean consumers have become more likely to be exposed to high-risk products.
- 2.12 Separately, the government has recently launched a consultation with proposals to reform exemptions in the Financial Promotions Order for high net worth individuals and sophisticated investors to ensure they are calibrated correctly. Further details can be found online.³ The FCA's marketing restrictions also contain exemptions which enable promotion to high net worth individuals and sophisticated investors where relevant conditions are met. The government notes that if the conditions for the Financial Promotion Order exemptions were updated in light of this recent consultation (for example, if the thresholds were increased) then the FCA may decide to consult on replicating some or all of these updates to the exemptions in its own rules.

³ [Financial promotion exemptions for high net worth individuals and sophisticated investors: a consultation - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/consultations/financial-promotion-exemptions-for-high-net-worth-individuals-and-sophisticated-investors)

Chapter 3

The government's approach to regulating cryptoasset financial promotions

- 3.1 This chapter summarises the government's approach to regulating cryptoasset financial promotions set out in the consultation, the government's wider actions to regulate cryptoassets, and the government's rationale for regulatory intervention.
- 3.2 In the consultation, the government set out a proposed definition of 'qualifying cryptoassets', which will be added to the list of controlled investments in the Financial Promotion Order. The government also proposed to amend four existing controlled activities in the legislation to capture activities relating to qualifying cryptoassets.
- 3.3 Certain cryptoassets are already subject to financial promotions rules. These include security tokens, which are tokens with characteristics akin to specified investments, like a share or a debt instrument, as set out in UK legislation. Security tokens fall within the regulatory perimeter set by FSMA, under the Regulated Activities Order (the 'RAO'), and are captured by the Financial Promotions Order as controlled investments.⁴
- 3.4 E-money tokens, which are digital payment instruments that store value, can be redeemed at par value at any time and offer holders a direct claim on the issuer, are regulated under the Electronic Money Regulations 2011.
- 3.5 Unregulated cryptoassets (e.g. utility tokens and exchange tokens such as Bitcoin and Ether) are not currently subject to similar regulation for financial promotions. This measure, to expand the scope of the Financial Promotion Order to capture qualifying cryptoassets, will bring most of these unregulated cryptoassets into financial promotions regulation.

The government's approach to regulating cryptoassets

- 3.6 The government, in coordination with other authorities through the Cryptoassets Taskforce, has taken several actions with regards to bringing the cryptoasset market into regulation. This measure to expand the scope of

⁴ Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544)

the Financial Promotions Order to include cryptoassets forms part of the government's staged and proportionate approach to cryptoassets regulation, which is sensitive to risks posed, and responsive to new developments in the market.

- 3.7 In 2020, the government and the FCA implemented the Fifth Anti-Money Laundering Directive for cryptoassets, which brought custodian wallet providers and cryptoasset exchange providers into anti-money laundering and counter-terrorist financing regulation.
- 3.8 Government action to ensure the appropriate regulation of cryptoasset promotions is aligned with the government's wider proposals on the regulatory framework for stablecoins used for payments, which the government consulted on in January 2021. The government's January 2021 consultation focused on stablecoins as a priority area for further regulatory action given their potential use as a widespread means of payment, and the government will publish its response to the consultation and next steps shortly. The government's action to expand the scope of the Financial Promotions Order to include cryptoassets seeks to address a different set of risks and applies to a wider set of cryptoassets, particularly those used as a means of investment.

Rationale for intervention

- 3.9 In the consultation, the government outlined its rationale for the proposal to expand the scope of the Financial Promotion Order to capture cryptoassets. This rationale was supported by evidence from the Cryptoassets Taskforce 2018 report, which highlighted inaccurate promotions as a key risk to consumers in the market.⁵
- 3.10 Overall, most respondents were supportive of the government's proposed approach.
- 3.11 Many respondents specifically welcomed the government's risk-based, incremental approach to cryptoassets regulation, noting that increased regulation will aid industry growth and attract new consumers to the market. However, others expressed a view that this measure would be best implemented alongside a more comprehensive bespoke regulatory regime for cryptoassets.
- 3.12 In addition, several respondents questioned the rationale behind the intervention, citing the 2018 Cryptoasset Taskforce report as an outdated basis for assessing consumer risks.
- 3.13 Other respondents pointed to the FCA's decision to ban the sale of cryptoasset derivatives as evidence of disproportionate interventions in the industry. The government notes that the FCA's decision to take the measure forward after consultation was taken in line with the FCA's objectives which

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https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/752070/cryptoassets_taskforce_final_report_final_web.pdf

include both protecting consumers and promoting competition. The FCA has issued a detailed explanation of the rationale for the derivatives ban.⁶

- 3.14 In the time since the publication of the consultation, the government's view is that risks to consumers are likely to have increased, as evidenced by a number of factors including rising ownership of cryptoassets.
- 3.15 The FCA has conducted and published updated cryptoasset consumer research. The research supports the government's assessment of risks to consumers that was first identified by the 2018 Cryptoasset Taskforce report. The consumer research confirmed that cryptoasset ownership in the UK has continued to rise. The quantitative research fieldwork took place from 5 January to 24 January 2021.⁷
- in 2021, the FCA's estimate for the number of consumers holding cryptoassets rose to 2.3 million, a rise from 3.9% of the population to 4.4% of the population
 - however, public understanding of cryptoassets is declining, with only 71% of those who have heard of cryptoassets correctly identifying its definition; this is a drop of 4% from the FCA's previous consumer research, suggesting that some cryptoasset users may not fully understand what they are buying
 - the median holding of cryptoassets has similarly risen from £260 to £300
 - 31% of cryptoasset holders that saw an advert were encouraged to buy as a result
 - one in ten of the people who noted that they had heard of cryptoassets said they were aware of consumer warnings on the FCA website
 - of those that were aware of consumer warnings on the FCA website, 44% said the warnings had no effect in their plans to keep or purchase cryptoassets, while 43% said they were discouraged from buying
- 3.16 The government's view is that the evidence of risks to consumers provides a strong case for intervention, and the government intends to expand the scope of the Financial Promotions Order to include cryptoassets.

⁶ <https://www.fca.org.uk/news/press-releases/fca-bans-sale-crypto-derivatives-retail-consumers>

⁷ <https://www.fca.org.uk/publications/research/research-note-cryptoasset-consumer-research-2021>

Chapter 4

Regulatory scope

- 4.1 This chapter summarises how the government will expand the scope of the Financial Promotion Order in light of feedback to the consultation. This includes how the government intends to define those cryptoassets (to be known as 'qualifying cryptoassets') for the purposes of the Financial Promotion Order, such that they fall within scope of the regime, and how the relevant controlled activities and exemptions will be amended to apply to qualifying cryptoassets.
- 4.2 The consultation set out a proposed definition for qualifying cryptoassets, to be brought into the scope of the Financial Promotion Order as a controlled investment. The definition proposed in the consultation set out several criteria for a qualifying cryptoasset, including that it is fungible, transferable, not electronic money as defined in the Electronic Money Regulations, and not a currency issued by a central bank or public authority.
- 4.3 Overall, respondents were broadly content with the proposed definition. However, a few responses raised issues in relation to the definition of qualifying cryptoassets, which are discussed below.

Qualifying cryptoassets

Definitional complexity

- 4.4 Some respondents argued that the proposed concepts of fungibility and transferability, within the definition, were overly complex.
- 4.5 **The government considers that, in order to develop a regulatory framework that responds to identified risks and provides legal clarity, a clear legal definition is required.** The government considers that the terms are sufficiently clear and understood to be the basis for an eventual legal definition. However, the final drafting for that definition is still under development to ensure it delivers the policy effectively. Any eventual legislation is intended to be accompanied by any necessary FCA rules or guidance appropriate for the regime.

Transferability

- 4.6 A few respondents noted that including transferability in the definition for qualifying cryptoassets would make the effect of the measure too broad.
- 4.7 The government has examined the implications of the suggested definition in light of feedback from respondents and agrees that the transferability criteria could potentially include a wider set of tokens than intended, such as

digital vouchers and customer loyalty point schemes that are cryptographically secure. **The government intends to include a ‘transferability exclusion’ within the definition to ensure appropriate scope.**

- 4.8 The transferability exclusion will exclude tokens such as travel passes, lunch passes, and supermarket loyalty schemes that are cryptographically secure from the regime. It was not and is not the government’s intention to include such tokens within the scope of financial promotions regulation, because tokens with these characteristics do not typically give rise to consumer protection risks. The transferability exclusion will also distinguish between those tokens that are used specifically and only for payment to a vendor (not in scope), and tokens which can also be traded between users for speculation or other purposes (in scope). **The government’s view is that the inclusion of this additional limb in the definition will clarify the types of transferable tokens that are in scope.**

Fungibility

- 4.9 In the consultation, the proposed definition of qualifying cryptoassets was deliberately broad, intending to capture the most commonly used cryptoassets (such as Bitcoin), but with the intention of carving out non-fungible tokens, which are typically tokenised representations of a unique digital item, such as a photo or a video. Non-fungible tokens (often referred to as NFTs) can also be used as tokenised ownership of an array of other assets such as art, music, or online gaming tokens.
- 4.10 Non-fungible tokens were carved out because fungibility – a core characteristic of a range of regulated financial services products, such as stocks and bonds - is a characteristic HM Treasury considers makes a cryptoasset significantly more likely to give rise to consumer protection concerns. Further detail was set out at consultation (see para 4.23 – 4.25 of the consultation document). Unlike fungible assets which can generally be sold more easily and quickly, the sale of non-fungible tokens typically depends on the utility or unique value it gives the holder and is more akin to a digital collector item than financial services products.
- 4.11 Several respondents highlighted concerns with incorporating the concept of fungibility into the definition. Respondents noted the possibility that some non-fungible tokens can be purchased and sold purely for speculative purposes, such that similar risks may arise from both categories of token. A few responses noted the possibility that a fungible token could be ‘wrapped’ inside a non-fungible token in order to evade the regime.
- 4.12 The non-fungible token market has grown considerably in recent months and new types of non-fungible tokens have emerged which blur the boundary between financial services products and digital collector items. It is not the government’s intention to apply financial promotions regulation to non-financial products.
- 4.13 **The government has carefully considered whether fungibility should be included in the definition of qualifying cryptoassets, or whether to capture both fungible and non-fungible tokens within the regime. The government has decided to retain fungibility in the definition of qualifying cryptoassets,**

leaving non-fungible tokens out of scope, for a number of reasons. Firstly, as noted, non-fungible tokens may represent a wide array of different assets which might constitute non-financial services products. Additionally, as the non-fungible token market is evolving rapidly and remains at an early stage of development, the government does not yet have sufficient information on risks and use-cases. As such, seeking to bring non-fungible tokens into scope might have unintended consequences for the market. Instead, the government will continue to closely monitor market developments, and stands ready to take further legislative action if required.

- 4.14 Regarding the specific issue of token ‘wrapping’ raised by some responses, the government’s view is that a wrapped token (where a fungible token is wrapped inside a non-fungible token) could present key characteristics of fungibility, if it could be readily interchanged with other similar tokens. Ultimately the question of whether wrapped tokens would be captured depends on a case-by-case assessment. The government’s role is to set the regulatory perimeter and definitions which is supported and applied through FCA rules.

Hybrid tokens

- 4.15 Several respondents sought further clarity on the status of hybrid tokens and whether these tokens would fall within scope of the proposed regime. **‘Hybrid token’ is not a regulatory classification under the Financial Promotion Order. The question of how the regime applies to them will be determined by the classification of the token at the time the promotion is made. In any case, the government expects that promotions in relation to these tokens would be within scope as either relating to a qualifying cryptoasset or as another controlled investment.** This is because the statutory instrument will bring unregulated cryptoassets such as utility and exchange tokens into the scope of the financial promotions regime (provided they fall within the definition of ‘qualifying cryptoasset’), and security tokens are already captured as controlled investments in the RAO, and are therefore subject to the Financial Promotion Order.
- 4.16 Tokens that change over time will be treated by the regime in accordance with whichever characteristics they exhibit at the time that the promotion is issued.

Distributed Ledger Technology (DLT)

- 4.17 The government has reassessed the necessity of specifying the type of underlying technology a cryptoasset uses in a legal definition. While most cryptoassets currently use distributed ledger technology (DLT), it might be that this changes as the technology and industry evolve. **Therefore, the government proposes to remove the reference to DLT from the definition of qualifying cryptoassets. This will future-proof the definition for innovations in the underlying technology that cryptoassets utilise. This technology-agnostic definition is in line with the definition proposed by the government in its consultation on the regulatory treatment of stablecoins.**

Proposed scope of qualifying cryptoassets

- 4.18 In line with the policy set out here, the government intends to define the scope of 'qualifying cryptoasset' as any cryptographically secured digital representation of value or contractual rights which is fungible and transferable. The definition will exclude other controlled investments, electronic money under the Electronic Money Regulations 2011, and central bank money. The government also intends to exclude cryptoassets that are only transferable to one or more vendors or merchants in payment for goods or services.
- 4.19 The government emphasises that the proposed definition is provisional at this stage, and final drafting when the statutory instrument is laid before Parliament may be subject to change.
- 4.20 However, by providing an indication of the proposed definition, the government intends to provide industry with a sense of the scope of what is intended to be captured by the term 'qualifying cryptoassets', to aid industry understanding of how the government intends the regime to work.

Treatment of controlled activities

- 4.21 The Financial Promotion Order contains a series of controlled activities that capture the main business activities conducted by firms who deal in the controlled investments in the Financial Promotions Order. Not all of the controlled activities contained within the legislation are relevant to cryptoassets.
- 4.22 The consultation proposed to amend several Financial Promotion Order controlled activities to apply to qualifying cryptoassets. These activities are:
- dealing in securities and contractually based investments
 - arranging deals in investments
 - managing investments
 - advising on investments
 - agreeing to carry on specified kinds of activity
- 4.23 In the consultation, the government set out that these controlled activities best reflect the activities that cryptoasset businesses conduct in the UK, and are the activities most associated with misleading cryptoasset promotions identified by the FCA.
- 4.24 Prior to consultation, the government considered whether any activities unique to cryptoassets might need to be added to this list, in case they were not already contained in the Financial Promotion Order. For example, the government had considered whether activities relating to the provision of cryptoasset exchanges, cryptoasset ATMs, and airdrops might fall outside the above list of activities. The government considered that these activities could, depending on the particular circumstances, already be covered by the above set of controlled activities. **Following the consultation, the government continues to judge that there is not a case for adding any new controlled activities to the Financial Promotion Order.**

- 4.25 Some respondents queried the scope of activities covered by the Financial Promotion Order regime. In particular, respondents highlighted areas where they believed there to be omissions, including the coverage of crypto lending activities, decentralised finance (DeFi) protocols, peer-to-peer lending platforms, the provision of advice and activities relating to custodian wallets. These are explored below.

Cryptoasset lending and decentralised finance

- 4.26 Several responses to the consultation queried whether activities relating to cryptoasset lending and DeFi would be covered by the proposal to expand the scope of the Financial Promotion Order to capture qualifying cryptoassets.
- 4.27 Cryptoasset lending, where firms take on cryptoasset ‘deposits’ and pay ‘interest’ to ‘depositors’ from the income they receive from cryptoasset borrowers is an area of the market that has grown significantly since the publication of the consultation. Cryptoasset lending models are often complex, with models differing significantly on a case-by-case basis. **It is the government’s view that the controlled activities listed in paragraph 4.22 provide substantial coverage of the activities conducted by cryptoasset businesses. The government is seeking only to amend activities where strictly relevant to cryptoasset businesses, in order to avoid unnecessary and disproportionate amendments to the regulatory perimeter.**
- 4.28 Decentralised finance (DeFi) is a relatively new and fast-growing sector within the cryptocurrency landscape. DeFi platforms take the form of decentralised apps which are not controlled by a central authority, commonly known as/referred to as ‘dapps’. These dapps use a series of smart contracts to automate transactions, facilitating peer-to-peer lending, as well as peer-to-contract lending, borrowing or trading with financial instruments on a permissionless network. They include, for example, platforms that enable users to earn interest on their tokens by connecting token holders to other borrowers.
- 4.29 **The government believes that, in various instances, DeFi may be in scope. Whether certain cryptoasset lending activities or decentralised finance platforms are within scope of the regime ultimately depends on the activities being carried out and promoted.** As such, this will need to be considered on a case-by-case basis. The government will continue to closely monitor any developments in this market.

Wallets

- 4.30 Some responses questioned how activities relating to wallets would be captured by the proposal. In the consultation, the government proposed not to amend controlled activities relating to custody services.
- 4.31 The government continues to judge that the central activities causing consumer harm, and where misleading advertising is more commonly found, relates to the buying and selling of cryptoassets rather than the provision of custody activities which do not have the same risk profile as activities related to buying and selling.

Treatment of exemptions

- 4.32 The Financial Promotion Order contains a number of exemptions, which exempt certain types of communication from the financial promotion restriction. In practice, these exemptions enable unauthorised individuals or businesses to communicate financial promotions without requiring the approval of an authorised firm, and fall outside the regulatory perimeter of the FCA.
- 4.33 The exemptions listed in the Financial Promotion Order fall within three parts.
- the exemptions listed in Part IV apply to **all** controlled activities
 - the exemptions in Part V only apply to controlled activities and investments relating to insurance and deposit taking
 - part VI contains other exemptions, that apply only to **certain** controlled investments or **certain** controlled activities
- 4.34 In the consultation, the government set out that exemptions for qualifying cryptoassets should be consistent with the approach taken to exemptions for other controlled investments within the Financial Promotion Order. Responses to the consultation were broadly in agreement with the government's approach.
- 4.35 In addition, the government proposed to add a new exemption into the Financial Promotion Order. The proposed exemption would have carved out from the regime any promotions that simply state that a vendor is willing to accept or offer qualifying cryptoassets in exchange for goods and services. For instance, a shop with a sign saying 'we accept crypto' would fall into this category. **However, after considering consultation responses, the government's assessment is that such statements would not constitute an inducement to enter into investment activity, and would therefore be out of scope of the regime in any case. The government has therefore decided that this new exemption will not be added to the Financial Promotion Order.**
- 4.36 Some respondents commented that a specific exemption should be made for smaller businesses, due to the proposed regime being too expensive for some smaller firms to comply with. Others suggested an exemption for sales to institutional investors. Finally, some responses highlighted a concern that the existing Financial Promotion Order exemptions which carve out high net worth and self-certified sophisticated investors from the regime have historically been prone to abuse.
- 4.37 **The government's assessment is that its approach to exemptions should be consistent with the way that they are more broadly applied in the Financial Promotion Order and there is not a reason to take a different approach specifically for cryptoassets.**
- 4.38 Furthermore, applying these relevant exemptions in a consistent way will enable the government to create a measure that targets those who will most benefit from having access to fair, clear, and not misleading information.
- 4.39 Detail on the government's approach to exemptions is set out in Table 1.

Table 1: Approach to exemptions

Financial Promotion Order exemption	Applied to qualifying cryptoassets?
Part IV exemptions: this includes exemptions for investment professionals, communications to journalists, and communications to overseas recipients	Yes – these exemptions apply to all controlled activities, and will apply to all qualifying cryptoassets.
Part V exemptions: this includes realtime and non-realtime communications for relevant insurance activity	No – these exemptions only apply to activities relating to insurance and deposit taking, and are not relevant to cryptoassets.
Part VI exemptions: this includes self-certified sophisticated investors, high net worth companies, governments and central banks, and industrial and provident societies	Some - exemptions will apply where relevant given the existing scope of these exemptions. For example, we do not consider that Articles 48 (exemption for high net worth individuals) and 50A (exemption for self-certified sophisticated investors) apply as these exemptions only apply to promotions related to certain, specified, investments.

4.40 The exemptions contained in articles 48 and 50A of Part VI of the Financial Promotion Order for certified high net worth individuals and self-certified sophisticated investors will not apply to qualifying cryptoassets because these exemptions, which were originally implemented for capital raising purposes, apply only to a specific set of controlled investments set out in the legislation, namely unlisted securities. The full list of the controlled investments to which the exemptions in articles 48 and 50A may apply can be found in the text of the Financial Promotion Order.¹

4.41 As is currently the case in the application of the legislation in FCA rules, the FCA rulebook also contains a series of exemptions. The FCA will set out its approach to applying exemptions in its handbook rules to qualifying cryptoassets in its consultation.

Transition period

4.42 The government proposed not to have a transition period in legislation for the implementation of this measure in the consultation. However, responses to the consultation disagreed with this approach.

4.43 Given the clear feedback from much of industry that a transition period would be necessary to ensure suitable compliance with the regime, the government will introduce a six-month transition period for this measure.

¹ <https://www.legislation.gov.uk/uksi/2005/1529/article/50A/made>

Regime implementation and FCA rules

- 4.44 The government intends to put in place a suitable transitional period (approximately six months) from both the finalisation and publication of the proposed Financial Promotion Order regime and the complementary FCA rules.
- 4.45 As is already the case with the application of the Financial Promotion Order, the government and Parliament are responsible for setting the legal framework and scope of the regime, while firm rules and guidance will be determined by the FCA. The government understands that the FCA intends to consult on rules for cryptoasset promotions shortly.
- 4.46 In April 2021, the FCA issued a discussion paper which contained broad proposals on changes that could be made to their financial promotions rules for high risk investments. As set out in paragraph 3.10 of the FCA's paper, it is possible that the proposals for the regime for high risk investments would be applied to cryptoassets, provided that Parliament approves the statutory instrument to expand the scope of the Financial Promotion Order to capture qualifying cryptoassets. Further information on the details of these proposals can be found on the FCA website, and they provide a high-level indication of the FCA's potential approach to rules for cryptoasset financial promotions.²

² <https://www.fca.org.uk/publications/discussion-papers/dp21-1-strengthening-financial-promotion-rules-high-risk-investments-firms-approving-financial-promotions>

Annex A

Summary of consultation responses

The below annex sets out further detail regarding responses to the consultation, and is intended to supplement the key points of feedback – and government response – set out in the main body of the response, above.

Assessment of regulatory scope and definitions

1. Do you have any comments on the proposed definition of qualifying cryptoassets?

In general, responses agreed with the proposed definition of qualifying cryptoassets, but several respondents noted that further clarity would be required to ensure appropriate application of the regime. Responses touched on several key themes:

Complexity: other respondents noted concern that the definition would be too complicated for consumers and businesses to understand.

While the government acknowledges the complexity of the definition, this reflects the diverse nature of cryptoasset market, which encompasses a wide range of tokens which vary in form and function. A precise legal definition is also needed to ensure there is a clear, well-defined perimeter in financial services regulation.

Hybrid tokens: hybrid tokens were highlighted as an area of omission.

As set out in chapter two, the government believes hybrid tokens (e.g. where a token may begin as a security token, before evolving its design to become a utility token) may fall within the scope of this regime. Hybrid token' is not a regulatory classification under the Financial Promotion Order. The question of how the regime applies to them will be determined by the classification of the token at the time the promotion is made.

Fungibility: It was suggested that the criteria proposed in the definition of fungibility and transferability were too confusing for consumers to effectively understand the difference.

A number of respondents expressed a view that the inclusion of the term 'fungibility' in the consultation's definition may not offer the specificity and certainty required to determine which cryptoassets fall within the scope of the regime. These respondents noted that there is little certainty that a non-fungible token will always retain that characteristic. Some raised concern that the definition could give rise to 'wrapping' – whereby a technically fungible token is wrapped within a non-fungible

token in order to evade the regime. The government believes that these type of ‘wrapped’ non-fungible tokens would need to be reviewed on a case-by-case basis to determine whether they are captured by the regime.

Further, one respondent drew the government’s attention to the possibility that some technically non-fungible tokens are being purchased and sold purely for price speculation purposes, making the separation of fungibility and non-fungibility less clear. As set out in chapter three, the government will continually assess any new and emerging risks in the market, and stands ready to respond to them if needed.

Transferability: attention was given by respondents to the issue of transferability, noting that in some circumstances, a technically non-transferable token could be used as a transferable token within a closed but large digital ecosystem (such as an e-commerce platform), with the potential to cause consumer harm.

The government has listened to the concerns of consultation respondents, and has chosen to add additional text to the definition of qualifying cryptoassets (please see chapter four).

Implementation: it was noted that this measure would be best implemented alongside the broader regulatory framework for cryptoassets. The government’s sequencing rationale is set out in chapter three.

2. Do you agree that the correct tokens have been excluded from scope under this proposal?

Exemptions: most of the responses to this question asked for further clarity on the proposed exemptions to the regime. Some responses argued that smaller firms and new entrants to the market should be made exempt, where they could apply the regime on a voluntary basis. While the government recognises that the relatively new nature of the cryptoasset market will result in some small firms being brought into the perimeter, this is necessary because both small and large firms could pose a risk of consumer harm. Because this regime is being introduced in response to risks to consumers, smaller firms must also be subject to the regime. In addition, smaller firms are not exempt from the wider financial promotions regime, and the government does not believe there to be a reason why cryptoassets should divert from this approach. The government’s full approach to exemptions is set out in chapter four.

Proportionality of approach: another response commented on the proportionality of the measure, drawing on the example of foreign exchange (FX) spot markets as an area presenting a similar level of risk, without similar government scrutiny. While other types of investment do present risks to consumers, the government is particularly concerned about the pace of innovation in the cryptoasset industry, where novel risks are emerging.

As set out in the 2018 Cryptoasset Taskforce report, cryptoassets pose a range of substantial risks to consumers, which stem from consumers purchasing unsuitable products without having access to adequate information; from fraudulent activity; and from the immaturity or failings of market infrastructures and services.

Consumers may suffer unexpected or large losses without regulatory protection as a result of buying cryptoasset products that are not suitable for their needs, or buying these products while being unaware of the associated risks. The high volatility of cryptoassets, which may attract investors, can also lead to substantial losses. Consumers may also invest in products that are poor value due to unclear price formation and pricing practices, high fees and difficulty in assessing fundamental value. Investment in cryptoassets could also represent an opportunity cost for some consumers, who might forego another, potentially more suitable, investment to purchase a cryptoasset product.

Payment tokens: a number of respondents argued that because certain tokens are not intended to function in the same way as bonds or stocks, but instead be used for payments, they should be made exempt.

The government considers that hybrid utility and exchange tokens can also present a range of risks to consumers and therefore maintains its position that they should remain in scope. The promotion of e-money tokens is separately regulated, ensuring consistency.

3. In your view, which of the controlled activities in Part 1 of Schedule 1 to the FPO correspond most closely to activities undertaken by firms in the cryptoasset space? Which firms are undertaking these, and what services are they providing in particular?

4. Do you agree that the list of controlled activities under the FPO given at paragraph 4.22 best captures the activities undertaken by firms in the cryptoasset space which facilitate the buying, selling, subscribing for and underwriting of cryptoasset and whose activities are most associated with the risks this consultation seeks to mitigate? Do you agree that the government is therefore proposing to amend the correct set of controlled activities under the FPO?

There was agreement across the majority of responses that the following activities that the government proposed to amend were the most applicable to cryptoasset firms:

- dealing in securities and contractually based investments
- arranging deals in investments
- managing investments
- advising on investments
- agreeing to carry on specified kinds of activity

There was broad support that these activities should be amended to capture activities carried out in relation to qualifying cryptoassets.

Activities relating to custodial wallets: some respondents questioned the exclusion of activities specifically related to cryptoasset custodial wallet services.

While the government has chosen to not specifically capture wallet services, the government's analysis of the market in the UK indicated that there are very few providers solely offering custody services – it is instead more likely that custody services would be provided by firms offering bundled controlled activities alongside custody services. The government does not consider that the risk in relation to the promotion of custody services alone are the same as those of other activities, and that it is therefore not necessary to make amendments to capture custodial activities. Because safeguarding activities will not apply to qualifying cryptoassets, then a firm specifically promoting safeguarding services would not be caught for promotion of that activity, even if the promotion of their other activities could be, depending on the services offered. Further information is set out in chapter three.

Cryptoasset lending and de-centralised finance: many responses queried whether activities relating to cryptoasset lending, peer to peer lending, and de-centralised finance protocols would be captured within the regime. The government considers that cryptoasset lending and de-centralised finance will in some instances be captured by the regime, though these will need to be examined legally on a case-by-case basis by firms. More information is set out in chapter three.

Advice: Cryptoasset advice services were also raised as an omission. This is incorrect: the Government explicitly stated that 'advising on investments' would be one of the core activities carried out by cryptoasset firms.

6. Do you have any further comments on the proposed treatment of controlled activities?

Scheduling of regulatory change: many responses for this question discussed concern that adjusting the Financial Promotion Order separately from making corresponding changes to the broader regulatory perimeter will cause confusion for both regulated and unregulated firms. As previously stated, the Cryptoasset Taskforce identified risks within the industry that required urgent attention.

This regime is aimed at mitigating specific consumer harm risks identified by the Cryptoassets Taskforce. It is a separate regulatory action to the government's wider proposed framework for stablecoins, aimed at mitigating separate risks. The government and the FCA will endeavour to ensure that the rules and requirements relating to this regime will be made clear to industry prior to the commencement of the regime.

Others noted that frequent review will be required to ensure that the correct activities continue to be captured.

The Cryptoasset Taskforce has been convened by the government to monitor ongoing market developments; the Taskforce will continue to monitor and respond to emerging risks in the cryptoasset market.

Approval process for promotions: one respondent argued that the sign off process for these promotions is likely to prove expensive and time consuming for firms.

While the government acknowledges that firms will be expected to bear costs of compliance as a result of this measure, we consider that the benefits to consumers justify these costs. The government is proceeding with this measure principally to improve the quality of information consumers are given prior to purchase, to ensure that consumers purchase cryptoassets while being suitably informed about their potential risks. Furthermore, this is the case for other financial services products in the regime, and the government does not judge there to be a reason why cryptoasset firms should be treated differently.

Social media promotions: social media marketing frequently appeared as a concern of firms. Due to the inherently digital nature of cryptoassets, it was noted that delivering marketing on social media will make compliance a bigger problem, particularly if the advertisements derive from abroad and are targeted according to consumer search terms. Social media promotions that target UK consumers are required to be fully compliant with the financial promotions regime, regardless of the jurisdiction within which the issuer is based.

7. Do you have any views on the government's proposed treatment of exemptions?

While not all respondents offered a response to this question, those that did were largely content with the approach set out by the government. The government stated in the consultation that they would be taking a consistent approach to applying Financial Promotion Order exemptions to cryptoassets.

Some respondents expressed concern with how some exemptions are applied within the Financial Promotion Order more broadly, particularly regarding the high net worth and self-certified sophisticated investor exemptions that exist within Part VI of the Financial Promotion Order exemptions. These respondents noted that using these exemptions for qualifying cryptoassets might create a risk of regulatory arbitrage.

The government acknowledges these concerns – as set out in chapter four articles 48 and 50A will not apply to qualifying cryptoassets, in order to ensure the regime is as effective in its reach as possible, and is consistent with the regime for comparable activities.

8. Do you agree with the government's assessment of the risks in the cryptoasset market, as summarised and outlined in detail in the Cryptoassets Taskforce report?

The majority of responses received agreed with the government's assessment of the level of risk in the market.

Risk narrative: in one response, concern was raised that much of the narrative surrounding the risks related to cryptoasset purchase are anecdotal. There is a risk that the recent media coverage afforded to rapid price increases (and falls) of some cryptoassets could contribute to a partial or incomplete interpretation of the risks.

The government believes that since the publication of the consultation, the need for consumers to be well informed of the risks associated with purchase is more pressing, as cryptoasset ownership in the UK rises.

FCA derivatives ban: some respondents commented on the FCA's recent decision to ban the sale of cryptoasset derivatives.

The FCA is an independent body and its decision to take this ban forward is based on powers granted to the FCA under statute, pursuant to the FCA's objectives which include both protecting consumers and promoting competition in the interest of consumers.

Evidence for intervention: another respondent questioned the use of the FCA consumer survey as the evidential basis of the consultation, noting that a consumer regretting a purchase does not directly equate to economic harm of purchase. Additionally, several respondents similarly noted that, given the fast-growing nature of the market in the UK, the risk assessment in the 2018 Taskforce report will need updating.

The government's basis for this intervention is not predicated solely on the 2018 Cryptoasset Taskforce report; it is also informed by HM Treasury's own ongoing monitoring of the market, and FCA consumer research commissioned in 2019, 2020 and 2021, which highlighted a growth in cryptoasset ownership in the UK, as well as a decrease in public understanding of the risks. Further information on this research can be found in chapter one of this document.

HM Treasury will continue to work closely with the FCA, Bank of England and PSR as part of the Cryptoasset Taskforce to continually assess risks. The January 2021 consultation on the regulatory framework for cryptoassets, in particular stablecoins, is a product of this ongoing appraisal of the industry and risks arising from it by the Taskforce.

9. Do you agree with the government's assessment of alternative policy options?

In general, there was agreement with the government's assessment of alternative policy options, with a few exceptions.

Sunset clause: some noted that there should be a sunset clause included in the legislation to ensure it can be reviewed and revisited in light of the broader cryptoasset consultation.

The Cryptoasset Taskforce exists to continually assess the risks in the market, and the effectiveness of the legislation that regulates it. Further, the government's decision to pursue a staged approach to legislation will allow for an ongoing appraisal of the effectiveness of this measure.

Bespoke regime: others expressed a preference for a bespoke approach. While the government accepts that many other nations have chosen to draw up bespoke regimes for the treatment assets, the assessment of the Cryptoasset Taskforce

identified a series of specific risks to UK consumers. The government has chosen to pursue an agile approach to the regulation of cryptoassets, focusing on areas where the risk of consumer harm is most acute. This approach allows the government to support innovation, while ensuring that risks to consumers are robustly mitigated.

The government believes that the financial promotions regime provides a suitable basis to mitigate this risk to consumers from misleading advertisements, and that a bespoke approach for the treatment of cryptoasset promotions specifically would be duplicative of this regime.

Industry standards: a few respondents suggested the use of industry codes or voluntary standards as an option, or alternatively a publication of sectoral guidance, with a common disclosure to place on promotions.

The government believes that these options would not offer a sufficiently robust mitigation of the identified risks. This approach would also be inconsistent with the government's approach to similar potential risks arising in the context of financial service promotions for mainstream financial services.

Alternative legislative vehicles: another suggested alternative expressed by some respondents suggested that the best course of action would be to consult on expanding the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO) to designate cryptoassets as specified investments. Under this approach, firms would need to be authorised in order to carry out a range of cryptoasset activities.

The government's view is that while the RAO could in some respects serve as a suitable regulatory framework for cryptoassets, there needs to be an ongoing assessment of risks in the market, as well as a consideration of responses to the wider consultation before a decision is made. The government will be shortly setting out next steps relating to the wider regulatory regime for stablecoins.

10. Do you have any views on the government's proposal to not provide for a transitional period?

There was broad consensus in the responses on this question: almost all respondents agreed that there should be a transition period, to allow firms suitable time to adjust their compliance departments accordingly.

The government agrees with this reasoning set out by many of the respondents. There will be an intended transition period of six months introduced, from the finalisation and publication of the proposed Financial Promotion Order regime and the complementary FCA rules, giving businesses suitable time to ensure proper compliance with the regime.

11. Do you have any views on the proposed approach to territoriality?

While not all respondents chose to answer this question, in general responses agreed with the proposed approach.

The government does not propose to adjust the Financial Promotion Order's territorial scope, which currently applies to all firms in the UK and overseas which issue promotions to UK customers.

Boilerplate warnings: one respondent highlighted a risk that there could be a 'boilerplate' text added to overseas firms' websites and emails, stating that they are not directed at investors in the UK. The FCA, have appropriate powers to take action should they need to.

12. Do you have any additional comments to make on the proposed approach?

Authorised persons: only a few respondents chose to answer this question. The main concern raised related to who the 'authorised persons' willing to approve financial promotions would be. The government acknowledges this concern: while the separate consultation on the financial promotions regime sought views on how best improve the regime, the focus of this measure is primarily to protect consumers from risk.

The government acknowledges the possibility that the pool of authorised persons willing to approve the promotions of unauthorised firms may not be large, but considers this risk is justified by the importance of the measure more broadly.

The FCA will shortly consult on its rules for the implementation of this measure, which will in turn inform which firms will take on the role of approving promotions.

Impacts of the proposal

13. Promotions costs/challenges

- a. How many promotions annually would you estimate that your firm would need to have signed off by a firm authorised under FSMA?
- b. Do you have an estimate of the costs of (or qualitative assessment of the challenges involved in) redesigning promotions to make them compliant with the law?
- c. Do you have an estimate of the costs of (or qualitative assessment of the challenges involved in) having promotions signed off by a firm authorised under FSMA?

Most respondents chose to not answer this question, indicating that many companies did not have appropriate data to respond to these questions.

One response noted that they could not identify any existing authorised firm that would be willing to sign off promotions for decentralised finance projects. If there was a firm willing to do this, the firm noted, they would likely be a lone player and have a monopoly.

Estimation of costs: only limited data was received in response to this question asking respondents to estimate costs. A few respondents estimated annual promotions as being between 110-500 signed off annually, with the average costs of £100-200 per promotion redesign.

14. Comparative impacts on firms

- a. Do you anticipate that the proposed measure would impact some firms more than others? E.g. do some firms rely more heavily than others on promotions?

Risk to smaller firms: not all respondents chose to answer this question. In those that did, there was consensus in all the responses to this question that it would be smaller and less mature firms that would be presented with greater challenges by this regulation.

The government takes these concerns seriously. Any future regulatory framework will aim to balance supporting innovation in the industry with a need to protect consumers from risk. The government is willing to proceed with this measure as a necessary step to mitigate risks to consumers, despite the potentially uneven impact of the measure across industry. The government considers that in the longer term, this measure is likely to improve consumer confidence to the industry's benefit.

15. Market sizing and overall firm impacts

- a. Do you have an estimate of the number of firms that would be affected by this measure?
- b. Do you have estimates of the value of the cryptoasset market in the UK?
- c. Do you have estimates as to the annual turnover and/or profits of the average firm that would be affected by this measure?

Most respondents chose to leave this question blank, noting that they do not have accurate data to inform an answer to this question.

One firm noted that annual turnover and profits would be low relative to the type of firms that usually engage in financial promotions.

The government believes that this measure should apply to both small and large firms, as both can pose a risk to consumers.

One firm offered estimates:

- 10,000 firms affected, at a minimum
- estimated the UK crypto market to be worth in excess of £1 billion
- estimated the average annual turnover of these firms to be between £100,000 and £2.5m

16. Consequences for the UK market

- a. Do you have any views as to the impact that the above policy proposal, if introduced, would have on the cryptoasset market in the UK?

Many respondents chose not to answer this question. Of the responses received, there was no clear consensus.

Some respondents were of the view that the proposal will have a positive impact on the market, noting that with improved compliance and regulation comes increased adoption.

Other firms disagreed. They argued that the proposal will harm the UK market, and stifle smaller players.

While the government acknowledges the likely varying degrees of impact across the industry, as stated above, the government believes that this measure must be applied across the industry if it is to be effective in protecting consumers. It is important that, across the industry, consumers have access to fair, clear, and not misleading promotions, ensuring any decision to purchase cryptoassets is made in full knowledge of the associated risks.