



HM Treasury

Managing the failure of systemic digital settlement asset (including stablecoin) firms:

Consultation

May 2022

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Chapter 1

Introduction

- 1.1 The government has made a firm commitment to place the UK's financial services sector at the forefront of cryptoasset technology and innovation. It is taking a staged and proportionate approach to cryptoasset regulation, which is sensitive to risks posed and responsive to new developments in the market. This approach will focus on stablecoins in the first instance given their potential to develop into a widespread means of payment.
- 1.2 Among other things, it is intended that this will create the conditions for issuers and service providers of stablecoins used as a means of payment to operate and grow safely in the UK, driving consumer choice and efficiencies. However, the government also considers it necessary to ensure appropriate, and proportionate, tools are in place to mitigate the financial stability issues that may materialise should a firm that has reached systemic scale fail. This consultation sets out the government's intention to deliver such tools in a timely fashion.
- 1.3 Since the initial commitment to regulate certain types of stablecoins, events in cryptoasset markets have further highlighted the need for appropriate regulation to help mitigate consumer, market integrity and financial stability risks.
- 1.4 In January 2021 HM Treasury issued [a consultation and call for evidence](#) inviting views from stakeholders on the UK regulatory approach to cryptoassets and stablecoins.¹ This set out the government's judgement that there is a strong case for bringing stablecoin with the capacity to be used for payments into the UK regulatory perimeter for payments.²
- 1.5 The government published its [response](#) to this consultation in April 2022 and confirmed its intention to bring forward legislation, when parliamentary time allows, that will be used to bring into scope of established regulatory regimes for electronic money and payments certain cryptographically secured digital representation of monetary value that are used for the purpose of making payment transactions.³

¹https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/950206/HM_Treasury_Cryptoasset_and_Stablecoin_consultation.pdf

² In scope activities were: issuing, creating or destroying asset-linked tokens; creating or destroying fiat-linked tokens; value stabilisation and reserve management; validation of transactions; access; transmission of funds; safeguarding and administering assets belonging to a third party/or another; executing transactions in stable tokens; exchanging tokens for fiat money and vice versa.

³ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1066166/O-S_Stablecoins_consultation_response.pdf

- 1.6 This would be designed to bring stablecoin-based arrangements under the auspices of existing electronic money and payments regulatory regimes, which provide the Financial Conduct Authority (FCA) with powers to regulate and supervise firms engaged in relevant electronic money and payments activities.
- 1.7 In this response, the government also noted the need to manage risks related to the failure of a systemic stablecoin firm which either acts as a systemic payment system and/or is a service provider of systemic importance, and that the government anticipates broadening the definition of a payment system to include arrangements that facilitate or control the transfer of “digital settlement assets”. This would provide the Bank of England with powers to regulate systemically important payment systems and service providers as designated under Part 5 of the Banking Act 2009. A payment system may be designated as systemic where deficiencies in its design or disruption to its operation may threaten the stability of the UK financial system or have significant consequences for businesses or other interests.
- 1.8 For clarity, in this paper we use the broad term “digital settlement asset” (DSA) to refer to stablecoin of the type consulted on previously, together with wider forms of digital assets used for payments/settlement. We use the term “systemic DSA firm” to refer to systemic DSA payment systems and/or an operator of such a system or a DSA service provider of systemic importance. In the case of stablecoin, this might include – but is not limited to – the issuer of a stablecoin, a wallet, or a third-party service provider.
- 1.9 The failure of a systemic DSA firm could have a wide range of financial stability as well as consumer protection impacts. This could be both in terms of continuity of services critical to the operation of the economy and access of individuals to their funds or assets. Further work will be required to consider whether it would be appropriate to put in place a bespoke legal framework for the failure of such firms and, if so, its design. However, the government considers that it is important to ensure existing legal frameworks can be effectively applied to manage the risks posed by the possible failure of systemic DSA firms for the purposes of financial stability.
- 1.10 In advance of any consideration on the need for a bespoke legal framework for systemic DSA firms, HM Treasury considers an amended Financial Market Infrastructure Special Administration Regime (FMI SAR) to be the most appropriate vehicle through which to address the risks posed by the possible failure of systemic DSA firms which are not banks. Banks are catered for by separate pre-established regimes.
- 1.11 This consultation seeks the views of stakeholders on both the intention to appoint the FMI SAR as the primary legal framework through which to address the failure of a systemic DSA firm, as well as the necessary amendments that will be required to ensure the FMI SAR can operate effectively with regard to such a firm. Separately, HM Treasury will be consulting in the coming months on the regulatory perimeter for systemic payments firms at large.

Chapter 2

Proposed approach

- 2.1 Special Administration Regimes (SARs) provide for bespoke insolvency provision where the general administration process is not considered to be in the public interest. For example, where an additional or alternative objective is imposed on the administrator, who is normally expected to act in the best interests of the creditors. Two principal special administration regimes currently exist in UK legislation that could potentially be applied to the administration of a systemic DSA firm that is not a bank: the Financial Market Infrastructure Special Administration Regime (FMI SAR) or the Payment and E-Money Special Administration Regime (PESAR).
- 2.2 The FMI SAR was established to address the risks posed by the possible failure of payment systems recognised as systemic (for instance, Faster Payments or Bacs) where the government judged that disruption to or the discontinuity of such a system due to insolvency would not best serve the public interest given potential impacts on financial stability. In particular, severe disruption to the functioning of the wider financial sector and the real economy might ensue due to the volume and value of transactions processed by such systems on behalf of households and businesses. The FMI SAR, therefore, imposes an objective on administrators to pursue the continuity of a failed payment system's services ahead of the interests of its creditors and provides the Bank of England with powers of direction and oversight over the administrator to this end. For example, it must approve the administrator's proposals from the outset (and on a continuous basis) and has powers to direct the administrator to take or refrain from taking specified actions.
- 2.3 The PESAR was established to address the risks posed by the possible failure of payment and electronic money institutions, where the insolvency of such firms previously has resulted in lengthy delays in the return of customer funds. To this end, the PESAR provides administrators with an expanded toolkit to provide for, among other things, the prompt return of customer funds and provides the FCA with powers of direction over the administrator.
- 2.4 At present, there is arguably a lack of clarity as to which of the two regimes would apply in the case of the failure of a systemic DSA firm with potential negative implications for the efficacy of the subsequent management of such a failure. The government provisionally considers that despite both regimes having properties that could advantageously be applied in the case of a systemic DSA firm failure, neither would necessarily be able to properly address financial stability risks in their current form.
- 2.5 The government therefore intends to legislate, when parliamentary time allows, to establish that the appropriate SAR for systemic DSA firms (which are not

banks) will generally be the FMI SAR, and in the event of an overlap, the precedence of the FMI SAR over PESAR for systemic DSA firms that could fall in scope of both regimes.

- 2.6 The government considers the FMI SAR to be the most appropriate regime primarily because it considers the Bank of England, rather than the FCA, should be the lead regulator in the administration of systemic DSA firms. As lead regulator, the Bank of England will have powers of direction over an appointed administrator that will enable it to pursue its statutory role with regard to financial stability.
- 2.7 However, the government does not consider the FMI SAR, as it currently applies to systemic payment systems, as capable of addressing all of the financial stability risks associated with a systemic DSA firm's failure. Therefore, the government also intends to make suitable amendments to the FMI SAR as it applies to such DSA firms now brought into scope to ensure risks to financial stability can be addressed under the regime. It is the government's intention that the regime's application to those currently within its scope will remain unchanged.
- 2.8 The FMI SAR's primary objective focuses on continuity of services. In practice, this means that an administrator appointed under the FMI SAR will be required to direct their attention towards ensuring a firm can continue to operate. For traditional payment systems this is appropriate as the primary financial stability impact of such a firm's failure would arise from such a payment system ceasing to operate.
- 2.9 Unlike traditional payment systems, DSAs allow users to store value which is then used for the movement of funds between cryptoassets without transitioning into fiat money. As such, subject to the specific nature of the firm being addressed by the regime, continuity of service may not be sufficient to mitigate risks to financial stability arising from the failure of a systemic DSA firm, particularly where large numbers of individuals may lose access to funds and assets they have chosen to hold as DSAs. Therefore, the government intends to add to the FMI SAR an additional objective covering the return or transfer of funds and custody assets which may only be considered when the FMI SAR is applied in relation to systemic DSA firms, and to make any necessary further amendments consequential to this. This would allow administrators to take in to account the return of customer funds and private keys as well as continuity of service.
- 2.10 For the regime's proposed new objective to be operationalised effectively, the government intends to enable the Bank of England to direct administrators as to which objective should take precedence in an administration. This will ensure that the Bank of England is able to respond flexibly to the specific circumstances of a firm's failure so as to ensure the particular risk it presents to financial stability can be addressed. The government also intends to introduce specific regulations in support of the FMI SAR to ensure that it can operate effectively when applied to DSA firms, including so that the additional objective can be effectively managed by administrators. This is necessary because the existing FMI SAR rules and regulations were drafted solely with the FMI SAR's continuity of service objective in mind and may not provide administrators with the necessary framework to address an objective oriented towards protecting

consumers. The government intends that the way in which the regime applies to traditional payment systems will not be impacted by these changes, which will only apply where a DSA is involved.

- 2.11 Finally, in recognition of the regulatory overlap between authorities including with regard to consumer protection, the government considers it appropriate that the Bank of England shall be required to consult the FCA before it seeks a special administration order for a systemic DSA firm that is subject to regulatory requirements imposed by both the Bank of England and FCA, or directs administrators with regard to the regime's objectives. This seeks to ensure that the Bank of England appropriately considers the impact on consumers of any direction it issues to an administrator. This is aligned with the approach taken for other entities regulated by both the Bank of England and FCA.

Box 2.A: Questions for respondents

- 1 Do you have any comments on the intention to appoint the FMI SAR as the primary regime for systemic DSA firms (as defined at para 1.8) which aren't banks?
- 2 Do you have any comments on the intention to establish an additional objective for the FMI SAR focused on the return or transfer of customer funds, similar to that found in the PESAR, to apply solely to systemic DSA firms?
- 3 Do you have any comments on the intention to provide the Bank of England with the power to direct administrators, and to introduce further regulations in support of the FMI SAR to ensure the additional objective can be effectively managed, or what further regulation may be required?
- 4 Do you have any comments on the intention to require the Bank of England to consult with the Financial Conduct Authority prior to seeking an administration order or directing administrators where regulatory overlaps may occur?

Chapter 3

Responding to this consultation

- 3.1 Responses are requested by 2 August 2022. The government cannot guarantee that responses received after this date will be considered.
- 3.2 The document is available electronically at www.gov.uk/treasury. You may make copies of this document without seeking permission. Printed copies of the document can be ordered on request from the address below.
- 3.3 Responses can be sent by email to fmisar.stablecoin@hmtreasury.gov.uk. Alternatively, they can be posted to:

Resolution Policy Unit
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

- 3.4 When responding, please state whether you are doing so as an individual or representing the views of an organisation. If you are responding on behalf of an organisation, please make clear who the organisations represents and, where applicable, how the views of members were assembled.

Processing of personal data and confidentiality

- 3.5 This notice sets out how HM Treasury will use your personal data and explains your rights under the General Data Protection Regulation (GDPR) and the Data Protection Act 2018 (DPA).

Your data (Data Subject Categories)

- 3.6 The personal information relates to you as either a member of the public, parliamentarians, and representatives of organisations or companies.

The data we collect (Data Categories)

- 3.7 Information may include your name, address, email address, job title, and employer of the correspondent, as well as your opinions. It is possible that you will volunteer additional identifying information about themselves or third parties.

Legal basis of processing

- 3.8 The processing is necessary for the performance of a task carried out in the public interest or in the exercise of official authority vested in HM Treasury. For the purpose of this consultation the task is consulting on departmental policies or proposals or obtaining opinion data in order to develop good effective government policies.

Special categories data

- 3.9 Any of the categories of special category data may be processed if such data is volunteered by the respondent.

Legal basis for processing special category data

- 3.10 Where special category data is volunteered by you (the data subject), the legal basis relied upon for processing it is: the processing is necessary for reasons of substantial public interest for the exercise of a function of the Crown, a Minister of the Crown, or a government department.
- 3.11 This function is consulting on departmental policies or proposals, or obtaining opinion data, to develop good effective policies.

Purpose

- 3.12 The personal information is processed for the purpose of obtaining the opinions of members of the public and representatives of organisations and companies, about departmental policies, proposals, or generally to obtain public opinion data on an issue of public interest.

Who we share your responses with (Recipients)

- 3.13 Information provided in response to a consultation may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 2018 (DPA) and the Environmental Information Regulations 2004 (EIR).
- 3.14 If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence.
- 3.15 In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information, we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Treasury.
- 3.16 Where someone submits special category personal data or personal data about third parties, we will endeavour to delete that data before publication takes place.
- 3.17 Where information about respondents is not published, it may be shared with officials within other public bodies involved in this consultation process to assist us in developing the policies to which it relates. In this case, your responses will

be shared with the Bank of England and the Financial Conduct Authority (FCA).
Examples of these public bodies appear at:
<https://www.gov.uk/government/organisations>

- 3.18 As the personal information is stored on our IT infrastructure, it will be accessible to our IT contractor, NTT. NTT will only process this data for our purposes and in fulfilment with the contractual obligations they have with us.

How long we will hold your data (Retention)

- 3.19 Personal information in responses to consultations will generally be published and therefore retained indefinitely as a historic record under the Public Records Act 1958.
- 3.20 Personal information in responses that is not published will be retained for three calendar years after the consultation has concluded.

Your rights

- You have the right to request information about how your personal data are processed and to request a copy of that personal data.
- You have the right to request that any inaccuracies in your personal data are rectified without delay.
- You have the right to request that your personal data are erased if there is no longer a justification for them to be processed.
- You have the right, in certain circumstances (for example, where accuracy is contested), to request that the processing of your personal data is restricted.
- You have the right to object to the processing of your personal data where it is processed for direct marketing purposes.
- You have the right to data portability, which allows your data to be copied or transferred from one IT environment to another.

How to submit a Data Subject Access Request (DSAR)

- 3.21 To request access to personal data the HM Treasury holds about you, contact:

HM Treasury Data protection Unit
G11 Orange
1 Horse Guards Road
London
SW1A 2HQ
dsar@hmtreasury.gov.uk

Complaints

- 3.22 If you have any concerns about the use of your personal data, please contact us via this mailbox: privacy@hmtreasury.gov.uk.

3.23 If we are unable to address your concerns to your satisfaction, you can make a complaint to the Information Commissioner, the UK's independent regulator for data protection. The Information Commissioner can be contacted at:

Information Commissioner's Office

Wycliffe House

Water Lane

Wilmslow

Cheshire

SK9 5AF

0303 123 1113

casework@ico.org.uk

3.24 Any complaint to the Information Commissioner is without prejudice to your right to seek redress through the courts.

HM Treasury contacts

This document can be downloaded from www.gov.uk

If you require this information in an alternative format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

Email: public.enquiries@hmtreasury.gov.uk