

## Financial Conduct Authority (FCA) Discussion Paper 23/4 on Regulating cryptoassets Phase 1: Stablecoins

### - Key Takeaways -

GDF convened its members to analyse the Financial Conduct Authority (FCA) Discussion Paper (DP) 23/4 on Regulating cryptoassets Phase 1: Stablecoins. GDF's response to this DP looks to provide suggestions of areas where further consideration and clarity may be needed for the creation of an appropriate and effective stablecoin framework in the UK. GDF worked with its members to identify five key areas that may require further drafting consideration or additional guidance for purposes of clarity, proportionality, and effective implementation:

1. **Proposed reconsideration of the treatment of overseas stablecoins;**
2. **Further consideration of the practical implementation of the 'payments arranger';**
3. **Additional guidance on custody requirements;**
4. **Further consideration of the reconciliation requirements; and**
5. **Further consideration of the recommendations for backing assets.**

This document outlines the key takeaways across the five themes, condensing the crucial considerations detailed in each of these principles for readers' ease of reference.

#### *1. Proposed reconsideration of the treatment of overseas stablecoins*

##### *Key Takeaways*

- **Support for the FCA Granting Use of Overseas Stablecoins:** GDF remains supportive of the FCA and their considerations of how to position the UK globally with regards to overseas stablecoins. We are supportive of the FCA granting the ability for overseas stablecoins being used in the UK where the appropriate safeguards are in place.
- **Different Overseas Stablecoins May Require Unique Treatment:** We would also urge consideration of the different types of stablecoins that may exist. There may be some overseas stablecoins that are sterling backed, but there are also likely to be many that are not sterling backed. We would encourage the FCA to consider what requirements may or may not be appropriate for different types of stablecoins. Further to this, different types of stablecoins may not be appropriate for UK retail consumers but may serve a different purpose in wholesale markets.

#### *2. Further consideration of the practical implementation of the 'payments arranger'*

##### *Key Takeaways*

- **Clarity on Exclusivity is Needed:** While we are supportive of the ability for overseas stablecoins to be used in the UK, further clarity is required on what kind of exclusivity may or may not apply to the arranger. GDF members raised concerns that if this not a contractual relationship it could result in an increase in risk for both sides.
- **Payments Arrangers May Give Rise to New Risks:** GDF would encourage consideration of the risk of trust and reliability of the arranger. For the arranger, they are taking on a reputational risk. In addition to this, under this proposal, a payment arranger could potentially have liability for an overseas stablecoin for which it has no responsibility over or ability to influence outcomes. For the overseas issuer there would also be the potential risk of a captive audience, (e.g., they could become a customer of the

arranger who are then reluctant to substitute one arranger with another, because of the high cost (in terms of discomfort, effort, and/or money) involved in switching.)

### ***3. Additional guidance on custody requirements***

#### *Key Takeaways*

- **Seed Phrases and Other Technical Aspects Should be Considered Alongside Private Keys:** GDF would encourage the FCA to consider technical requirements beyond those for private keys, such as seed phrases. We believe it would be appropriate to address the notion of broad methodologies and technical aspects of control over the asset. This is an equally important protection to be managed and we would encourage the FCA to include guidance on this in their final framework.
- **Ownership and Recordkeeping Technicalities Should be Addressed:** We would encourage the FCA to consider what additional requirements may be needed to effectively preserve ownership rights with omnibus wallets. Furthermore, when transactions are carried out off-chain, we would encourage the FCA to clarify in the final framework whether a register kept by the custodian would be sufficient as a safeguard.
- **Overseas Custody Considerations:** GDF would encourage the FCA to provide further clarity and additional guidance to technology providers, particularly those situated in other jurisdictions than the UK, on how they would be able to assess whether they are undertaking custody services or not in the UK, and what would be the consequence of undertaking such services (in particular, whether a technology provider would need to obtain a license in the UK even if its providing its services from/in other jurisdictions).

### ***4. Further consideration of the reconciliation requirements***

#### *Key Takeaways*

- **Greater Flexibility is Encouraged:** GDF would encourage a less restrictive reconciliation requirement and for the public and private sector to work together to determine what data would be most useful to share in real time. For example, where off-chain records are used, and these off-chain records are held on traditional systems. Firms would need to ensure that their existing systems are capable of interacting with the blockchain on a real-time basis. If this is not feasible, then some flexibility may be beneficial as record keeping systems continue to evolve with new technology. GDF is supportive of an approach similar to CASS 6.6.44 R which provides for a more flexible and proportionate approach to frequency of reconciliations.

### ***5. Further consideration of the recommendations for backing assets***

#### *Key Takeaways*

- **Flexibility and Consideration of UK Competitiveness is Crucial:** While we agree with the importance of high-quality liquid reserves as backing assets, we believe that some aspects of the current proposals are slightly restrictive and may not account for all of the options available to safely manage reserves and the many different ways that stablecoins may be used. For example, other stablecoin proposals in other jurisdictions (such as Hong Kong) have presented alternative approaches that set a more flexible standard for backing assets. We would encourage the FCA to consider how flexibility presented in other jurisdictions may affect UK competitiveness in the market.
- **Specific Arrangements May Require More Flexibility:** There are cases where more flexibility may also be warranted in order to support the varying types of arrangements that exist in the market. For example, short-dated reverse repurchase agreements overcollateralized by government debt instruments present an important alternative that can help provide liquidity and manage credit and duration risk. For these, as well as other unique arrangements it may be appropriate for the framework to support alternative arrangements for backing assets.