

Consumer protection in view as cryptoasset activities brought into scope

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Introduction

In April, the UK Treasury published new measures to create a regulatory regime for cryptoassets in the UK. The FCA then published a Discussion Paper, describing how it proposes to regulate certain activities of cryptoasset trading platforms and intermediaries.

In most cases, cryptoassets are not regulated in the UK outside the financial promotion rules, with the exception of those which qualify as e-money, transferable securities or other specified investments. The Treasury's new measures set out a definition for 'qualified cryptoassets', which will be subject to the new regime. Qualified cryptoassets are all transferable and fungible cryptoassets (including stablecoins) that were not previously regulated as specified investments or in any other way (for example, as e-money).

A range of activities involving qualified cryptoassets will be regulated, including issuance of stablecoins, safeguarding, dealing as principle, dealing as agent and staking. The Treasury has proposed that only activities directed towards retail customers should be subject to authorisation. This means that activities aimed at institutional clients are intended to be out of scope. Stablecoin issuance will be regulated only if it is carried out in the UK.

No access to UK markets without authorisation

According to the Discussion Paper, the FCA is going to require Cryptoasset Trading Platforms (CATPs) to establish a branch or subsidiary in the UK to be authorised to provide cryptoasset services. However, if a foreign entity merely sets up a branch in the UK, the FCA is unlikely to give authorisation for the CATP to serve retail clients in the UK, due to limited visibility of its prudential arrangements in its home jurisdiction.

In traditional finance, trading venues do not generally enable direct retail access to their platforms. However, this is relatively common for CATPs and so the FCA is proposing that it enforce specific rules for CATPs that enable retail access to address their idiosyncratic risks. These include requirements for disclosures regarding activities' risks and customers' rights, and customer profiling. The regulator also plans to introduce specific rules for algorithmic trading, automated trading and market making.

CATPs will be allowed to operate on a non-discretionary trading basis only. The FCA expects that the matched principal – matching orders from buy and sell sides as middleman – will be the most common approach that platforms take. CATPs would not be allowed to trade as principals on their own platforms, and the risks associated with CATPs trading on other platforms are also being assessed by the regulator.

Finally, the FCA also highlights potential conflicts of interest (COIs) in CATPs' issuance activities and is considering whether a mandatory legal separation between issuers and CATPs is necessary.



For cryptoasset intermediaries, the FCA's focus is on enhancing customer understanding, client categorisation, and managing COI risks. The FCA plans to introduce best execution rules for retail cryptoasset clients, especially when the cryptoasset is traded on a UK-authorized platform. For non-retail clients, the best execution rule may still apply to professional clients, depending on the transaction, but they do not apply to eligible counterparties.

From excessive risk taking to consumer protection in cryptoasset borrowing

The regulator is expecting to require cryptoassets lenders to conduct creditworthiness assessments and comply with forbearance and arrears arrangements. In addition, the FCA intends to put limitations on collateral top ups (when the collateral does not meet the borrowed amount due to volatility) and to require firms to seek express consent from retail consumers while carrying out top ups.

For both borrowing and lending, notably, the FCA plans to introduce disclosure and appropriateness assessment requirements and to address COI risks will put limitations on platforms' use of their own tokens for lending.

It is also worth noting that the regulator plans to restrict use of credit to purchase cryptoassets, excluding stablecoins. This restriction may include banning the use of credit cards to directly buy cryptoassets or the use of credit line provided by an e-money firm to achieve the same result.

What should firms do?

The Treasury and FCA are still early in the process of finalising and implementing cryptoassets regulation, however there are steps that firms can and should take now to ensure that they are ready. Those that provide any services involving cryptoassets should assess whether their activities are caught by the proposed regulations. If they are, the next step should be to conduct a gap analysis, determining what remedial action is needed and the timeline for this to be completed.