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3 KEY DEVELOPMENTS

May 2022: This month's edition we have articles from David McIlroy, Lloyd Maynard and Clyde Darrell. This article will discuss the Crypto Crash, the Business Banking Resolution Service and the FCA Authorisation Post-Brexit.

The Crypto-Crash and the Regulation of Stablecoins

On 12 May 2022, Terra, the third largest stablecoin collapsed. Its fall dragged down Tether, the largest stablecoin, and also affected the price of the biggest cryptoassets, Bitcoin and Ethereum. Tether, Bitcoin and Ethereum have recovered to some extent. Terra is junk (now worth just a fraction of a cent).

Keen-eyed readers will have noticed that I called Bitcoin and Ethereum cryptoassets not cryptocurrencies. The reason is that, at present, the primary reason for holding Bitcoin and Ethereum is to speculate, not to make payments (though some crypto enthusiasts say that the next Bitcoin halving in 2024 will change that). The conventional asset class Bitcoin and Ethereum most closely resemble is investments not currencies.
Stablecoins, like Terra and Tether are designed differently. Their value is supposed to be pegged to a fiat currency (most often the US dollar) or to a commodity such as gold or to a basket of assets. As the name suggests, the value of such stablecoins is supposed to remain stable, tracking the value of the assets to which they are pegged. What

happened on 12 May 2022 was that speculators tested whether the price of Terra and Tether could be driven below the peg. In the case of Terra, the peg broke and the price collapsed. Put simply, there were not enough real, liquid assets available to the promoters of Terra and not enough faith in Terra from other investors to keep Terra pegged at par with the US dollar. Tether's price dipped to 0.95 cents but ultimately stabilised (just).

Since readers of this blog are looking for legal advice not investment advice, why does any of this matter? It matters because the likely effect of the crypto-crash is to have accelerated efforts towards the increased regulation of stablecoins and the development of central bank digital currencies (CBDCs). The crypto-crash coincided with the FCA's Crypto-Sprint event, to which it had invited industry insiders to discuss the future shape of its regulation. In the UK and the EU, stablecoins which can be redeemed against the issuer for a single fiat currency are already e-money subject to the Electronic Money Regulations 2011. We will either see the UK and the EU move in lockstep to regulate more forms of stablecoins as e-money or we will see competition between the regulators to bring in regulation first. The UK's intention to lead in this area had

already been made clear by John Glen MP in a keynote speech on 4 April 2022: https://www.gov.uk/government/speeches/keynote-speech-by-john-glen-economic-secretary-to-the-treasury-at-the-innovate-finance-global-summit

Effective regulation of stablecoins has, on the one hand, the potential to move stablecoins into the mainstream as a payment method. Their use will therefore be subject to the Payment Services Regulations 2017. However, on the other hand, it will mean that stablecoins operate wholly differently from the original dreams of those who saw Bitcoin and other cryptocurrencies as freeing money from the control of the state.
The increased regulation of stablecoins is also going to have a knock-on effect on the regulation of other crypto-assets. The UK authorities are already thinking about how to implement plans to regulate the advertising of "qualifying crypto-assets" and further rules can be expected. There will be a new regulatory code, the only question is how extensive it will be. The future may be digital, but there will still be red tape.

DAVID MCILROY (1995 Call)

David is the Head of chambers at Forum chambers and specialises in banking and financial services law, commercial law, and professional negligence.

For more information about David McIlroy see his profile here: https://forumchambers.com/our-people/david-mcilroy/

The Business Banking Resolution Service: a slow start in the resolution business

In 2018, a business client came to me for advice concerning an authorised push payment fraud ("APP Fraud"). A convincing fraudster had telephoned the client's office and informed a member of staff that their business account had been compromised by fraudsters. The company was advised to transfer as much of the remaining balance of the account into a "safe account" to protect it from further theft. That safe account of course belonged to the fraudster. The client acted upon the advice and unfortunately lost more than £300,000.

APP Fraud is an increasing phenomenon. Many business customers consider that banks ought to be able to recognise and intercept payments that have the hallmarks of APP Fraud, whether by reference to the exceptionally high value of payments, or the unusually high number of payment transactions over a short period of time. My client shared that belief.

I advised the client on the law surrounding bank's liabilities for APP Fraud at that time[1]

[https://forumchambers.com/successful-court-of-appeal-judgement-for-david-mcilroy/

[1] The law on APP fraud has featured in this blog series in recent months, with Forum's David McIlroy involved in a key victory in the Court of Appeal - see here:

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and discussed the client's options in civil proceedings. The client did not meet the eligibility criterion for the Financial Ombudsman Service ("FOS"). But I was able to inform the client that there was a proposed 'dispute resolution scheme' being put in place by 7 UK banks in response to the Walker Review, of which its bank was one of them. It was hoped that once the scheme was operational, it might provide a cost-effective means of achieving recompense for the bank's response to the APP Fraud.

In 2018, it was expected that the 'dispute resolution scheme' would deal with historic disputes that fell outside of FOS jurisdiction (for example, relating to the mis-sale of interest rate hedging products, provided that the customer had not been part of the Review of the sale of those products) and contemporary disputes relating to SMEs who were too big to complain to FOS. Those businesses typically have a balance sheet of up to £7.5 million or turnover of up to £10 million. Stephen Jones, the CEO of UK Finance, had said that the banks were confident that c60,000 customers would be eligible for the 'dispute resolution scheme' and so 99% of small businesses would have access to alternative dispute resolution (between FOS and this new scheme).

The envisaged 'dispute resolution scheme' has since been established as the Business Banking Resolution Service ("BBRS"). It provides independent dispute resolution services for disputes arising between SMEs and 7 banks (Barclays, Danske Bank, HSBC, Lloyds Banking Group, RBS Group, Santander UK plc and Virgin Money), who are believed to have paid between £23m - £30m to establish it.

Since the pandemic, BBRS has shifted its attention to dealing with complaints concerning the Coronavirus Business Interruption Loan Scheme ("CBILS"). There have been some 60,000 CBILS loans issued to businesses since the pandemic. Complaints are expected to centre around those businesses who have been refused a CBILS loan, or where their bank has refused to vary the terms of the loan due to changing conditions.

However, the BBRS has had a slow start to the resolution business. On 31 May 2022, BBRS released its reporting data from 15 February 2021 to 30 April 2022.[2] The data shows that BBRS has 148 live cases out of a total of 792 registered cases. It has produced determinations of only 8 complaints resulting in 6 matters which received financial redress. Those 6 cases include complaints where a business was awarded modest financial redress for distress and inconvenience. The report further suggests that the anticipated 60,000 eligible business customers is likely to be closer to 14,000 customers, of which up to 10% (1,400) are likely to complain.

On 21 May 2022, the Times Newspaper reported that Cat MacLean, a partner at MBM Entrepreneurial Business Lawyers, resigned from her membership of BBRS's SME Liaison

] a case which has recently been analysed by Ruhi Sethi-Smith, see here: [https://forumchambers.com/app-fraud-the-long-road-to-reimbursement/].

[2] See here: https://thebbrs.org/news/bbrs-reporting-data-as-of-the-close-of-business-30-april-2022/ last accessed Monday 13 June 2022.

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panel.[3] She is quoted as saying in her resignation letter that the BBRS was "completely defective" and that to remain part of BBRS would risk her being "complicit in a cover-up." It was also reported in May that Kevin Hollinrake MP, a member of the Treasury Select Committee, had criticised the BBRS's narrow eligibility criterion as being overly restrictive and called for BBRS to be scrapped.[4]

Last month my business client returned to me. Since 2018 it had followed the trajectory of BBRS and attempted to benefit from the scheme when it went live. Sadly, it fell outside of its eligibility parameters. It is now contemplating taking up proceedings in civil litigation, following positive recent developments on the law concerning the Quincecare duty.

It therefore appears that, despite the best intentions of UK Finance and the 7 participating banks, BBRS is unlikely to be a helpful forum for many large SME customers with banking services disputes. If you or your client is the victim of APP fraud or has other banking services complaints, Forum's barristers are well-placed to assist you through the litigation process with a view to a positive outcome.

Lloyd Maynard (2010 Call)

Lloyd is a member of Forum Chambers' commercial litigation, financial services and professional negligence teams.

For more information about Lloyd Maynard see his profile here: https://forumchambers.com/our-people/lloyd-maynard/

FCA Authorisation Post-Brexit: Branch or Subsidiary?

During the Brexit transition period, EEA financial services firms established in any EEA member state were entitled to use the passporting regime, introduced by the UK Government, to establish a branch or provide services in the UK without being authorised by the FCA. This passporting regime ended on the 31 December 2020 and 1 January 2021 saw the introduction of the Temporary Permission Regime ("TPR").

The aim of the TPR was to allow EEA-based firms that were passporting into the UK at the end of the transition period (31 December 2020) to continue operating in the UK within the scope of

[3] See article here: https://www.thetimes.co.uk/article/lawyer-cat-maclean-quits-completely-defective-banking-compensation-scheme-283blrxhd - there is a subscription payable to access. Last accessed Monday 13 June 2022.

[4] See article 'Business Banking Resolution Service (BBRS) has only effected six awards since launch, despite being established to handle anything up to a thousand SME disputes,' accessible here: https://smallbusiness.co.uk/mp-calls-for-banking-dispute-service-to-be-scrapped-2561434/ last accessed Monday 13 June 2022.

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their previous passport permission for a limited period after the end of the transition period. Given its temporary nature, the TPR is scheduled to last a maximum of 3 years from the end of the transition period (31 December 2023), subject to HM Treasury's power to extend the duration of the regime by increments of twelve months.

Firms operating within the TPR have been provided with 'landing slots' by the FCA which firms can use to apply directly to the FCA for full authorisation. There are 6 landing slots in 3-month blocks the first of which started in July 2021. The FCA have intimated that all applications will have been received by December 2022 with all applications completed by December 2023.

As part of a firms' application for authorisation, a key consideration for a firm accessing the UK market will be to identify what sort of establishment they wish to use. Most firms will have the option to either create a subsidiary or establish a branch. The FCA view the choice between a branch and subsidiary as important. This point was recently emphasised in a speech given by the CEO of the FCA, Nikhil Rathi (https://www.fca.org.uk/news/speeches/critical-issues-financial-regulation-fca-perspective):

> *"For businesses focussed in the UK, this will usually mean they want to set up an FCA authorised subsidiary. Most plans we've seen meet our expectations. But in some cases we've asked firms to think again.*
>
> *Where firms are not predominantly focused on the UK, and where we have good cooperation with the home state regulator, a branch may be appropriate.*
>
> *We have different powers over branches. So if you are a predominantly UK business, if most of your clients are here, it follows that your main entity should be here as well. This better protects UK based investors from harm and protects the integrity of the wider UK market."*

It is unsurprising that choosing a subsidiary is the FCA's preferred route where a firm has a larger footprint in the UK. The FCA view regulating branches as more difficult and a greater risk to its regulatory objectives especially where a particular firm is predominately based overseas. Therefore, international firms, for example, who apply for authorisation as a branch can expect greater scrutiny of their applications for authorisation (https://www.fca.org.uk/publication/corporate/approach-to-international-firms.pdf) :

> *To account for this, when assessing an international firm against the relevant minimum standards, we will have regard to*

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> *whether there is a heightened potential to cause harm from the activities being undertaken from a branch and whether the risks can be adequately mitigated. We will also consider the nature and scale of the activities the international firm intends to conduct from outside the UK. Individual applications will be considered on a case-by-case basis, taking into account all relevant factors by reference to the threshold conditions.*

Firms who have already applied for authorisation during their landing slot or those who are currently applying, will have, no doubt, already been advised on the significance of choosing the appropriate establishment when applying for authorisation.

For those whose landing slot is approaching, it is important that careful consideration is given to how it intends to operate within the UK market post-authorisation. Questions such as how much of the UK market will the firm operate in, how much of the UK market will form part of the firms' overall business, how may 'boots on the ground' will the firm have and wwhat permission will I need, are some of the important questions that will need answering before any application for authorisation is made.

Given the above choice can be central to the success or rejection of a firms' application for authorisation, firms are encouraged to give this issue particular thought.

Clyde Darrell (2014 Call)

Clyde specialises in Financial Service Regulation and is currently advising and assisting an overseas bank on their post-Brexit application for FCA authorisation (part 4A permissions).

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