Written evidence submitted by Circle

CALL FOR EVIDENCE SUMMARY

Circle Internet Financial LLC ("Circle") appreciates the opportunity to provide this response to the House of Commons Treasury Committee Inquiry into the cryptoasset Industry. Circle commends the Committee for undertaking this timely inquiry as the U.K. Parliament seeks to define "digital assets" and establish a regulatory regime for payment stablecoins in the Financial Services & Markets Bill. The U.K. has the opportunity to be a global leader for digital finance and cryptoassets, so it is important to think strategically about the long-term opportunities for the United Kingdom. Circle would welcome the opportunity to participate in a future hearing and provide oral evidence to expand on this submission.

In this submission, Circle has answered all Inquiry questions posed and provided its unique perspective on these key points:

- Far from competing with traditional currencies, cryptoassets - in particular payment stablecoins - amplify the reach and utility of traditional currencies. This added utility can unlock economic growth and solve problems for businesses, consumers, and Britons excluded from the financial system. Privately issued cryptoassets can coexist with a potential pound sterling CBDC.

- The United Kingdom has a window of opportunity to maintain its position as a leading jurisdiction for global finance and innovation. However, the mixed messages from regulators and apparent misalignment between the Government and regulators impedes progress towards a stable business environment in which cryptoasset firms can make long term investment.

- Cryptoasset firms are both similar to and different from traditional financial institutions. Recognising what is novel about cryptoassets is necessary to effectively protect users while promoting innovation and economic growth. The U.K. must regulate cryptoassets in a holistic, balanced, and technology-neutral manner. Circle has proposed recommendations for specific policy areas of focus: payment stablecoins, cryptoasset firm registration, and advertising and promotions.

- Payment stablecoins have found unique success in catalysing activity in the crypto-economy. The special characteristics of payment stablecoins can find novel use cases in the mainstream economy, which can include increasing financial inclusion and payments optionality for businesses and consumers.

ABOUT CIRCLE

Circle is a global financial technology firm that provides internet-native payments and treasury infrastructure. We have developed foundational technology centred on payments and banking in the age of digital assets and the internet. Since Circle's founding, we have prioritised responsible financial services innovation and constructive engagement with regulators and public authorities around the world. Circle has a keen interest in the development of a transparent and well-regulated digital assets market that facilitates capital formation, maintains fair, orderly, and efficient transactions, and protects consumers. Partnership between the public and private sector is critical in developing technology-neutral, principled, activity-based regulation.

Circle is the sole issuer of USD Coin (“USDC”), one of the world’s largest digital currencies, with over $51 billion in circulation as of 9 September 2022; Circle has also recently launched Euro Coin (“EUROC”). Both fully-reserved digital currencies, USDC and EUROC have the benefits of blockchain-based digital assets – fast, inexpensive, transparent, highly secure, global, and interoperable value exchange over the internet – while remaining 1:1 fiat-backed, which removes the downside of extreme volatility that has plagued other cryptocurrencies. USDC is accessible across nine blockchains, is integrated as a settlement option in leading merchant and credit card networks, supports cross-border remittances, and is offered as a payment option by e-commerce platforms.

Additionally, Circle advances the frictionless exchange of financial value through its transaction and treasury services, which enable businesses and financial institutions globally to take advantage of the blockchain-powered global financial system. Circle is licensed to operate as a money transmitter or its equivalent in the United States where such licences are required. In addition, we have obtained a BitLicense from the New York Department of Financial Services (NYDFS) and are registered as a “Money Services Business” with the Financial Crimes Enforcement Network (FinCEN) in the United States.

INQUIRY QUESTIONS

1. To what extent are cryptoassets when used as digital currencies (such as Stablecoins) likely to replace traditional currencies?

From Circle's perspective, cryptoassets are not about disruption and substitution; instead, they enable optionality. USDC and EUROC are digital representations of dollars and euros that circulate on open, blockchain-based payment rails accessible to anyone. This is a marked contrast to existing systems that are proprietary, closed-source, and restricted in usage and development. Open payment rails allow anyone in the world to build powerful new products and services, accessible to anyone with an internet connection, atop crypto rails. Far from replacing traditional currencies, digital currencies build on them and extend their reach and advantages. When reliable, trusted digital representations of the dollar, the euro, and (potentially) the pound are onboarded to open public blockchains, the base currencies benefit from their distribution on blockchain rails. The currencies gain the characteristics of programmability, near-free transmission, near-instant final settlement, and global access. Payment stablecoins solve many of the shortcomings of traditional financial payment options including the high-cost of global transmission, limited interoperability, and limited operating hours.

The U.S. dollar has experienced a first-mover advantage in the stablecoin space. Even though the crypto-economy is global, 99% of payment stablecoins are dollar-denominated, a higher degree of dollar dominance than is observed in global trade.[1] These same benefits could accrue to the U.K. if more stablecoin supply was denominated in pounds. We are approaching a future state where privately issued stablecoins conform to regulations, have cyber and risk controls resistant to nation-state attacks, and support Visa-level transaction throughput and uptime without the 3% fee. Global companies, which see a future driven by payment systems optionality, are investing in enabling digital currencies and in companies like Circle.[2] The U.K. can lead that future and profit from the associated economic benefits, or it can perpetually play catch up.

In the U.K., providing for the use of payment stablecoins for day-to-day payments, as announced by the Government in April, can unlock opportunities for British businesses and consumers and strengthen the U.K.'s global competitiveness.[3] Around the world, the payments optionality enabled by stablecoins is being leveraged by small businesses, retail merchants, and large, traditional businesses alike. Just as the pound sterling serves as the base asset for trillions of dollars of real economic activity, a responsible, trusted, regulated stablecoin digital currency is the base asset for economic activity in the digital assets world. Where a regulated payment stablecoin exists, a host of other products can be built on top of it.

People around the world use payment stablecoins for a variety of use cases. In some countries, individuals are using USDC to preserve wealth, hedge against extreme inflation, and pay with dollars in local economies.[4] Circle has helped the legitimate, elected government of Venezuela distribute millions of dollars of desperately needed aid to the nation's front-line medical workers as they battled Covid-19 under horrendous conditions. Circle partnered with the Bolivarian Republic of Venezuela (led by President-elect Juan Guaidó), U.S.-based fintech Airtm, and the U.S. government to send the relief funds.[5] The joint initiative established a disbursement

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[1] Cryptodollars, Nic Carter, March 2022, page 20 and The International Role of the U.S. Dollar, Carol C. Bertaut, Bastian von Beschwitz, and Stephanie E. Curcuru, FEDS Notes, October 6, 2021.

[2] Circle raises $400m, expands partnership with BlackRock, Amelia Isaacs, *AltFi*, April 2022.

[3] Government sets out plan to make U.K. a global cryptoasset technology hub, HM Treasury, April 4, 2022.

[4] [4] Chileans Take Refuge in Stablecoins Amid Economic Turmoil, Marina Lammertyn, *Coindesk*, August 3, 2022 and Inside the crypto black markets of Argentina, Devon Zuegel, *Freethink*, August 13, 2022.

[5] Circle Partners with Bolivarian Republic of Venezuela and Airtm to Deliver Aid to Venezuelans Using USDC, Team Circle, November 20, 2020.

pipeline that leveraged USDC to bypass the controls that Nicolás Maduro's authoritarian government placed on Venezuela's financial system.

Likewise, businesses are leveraging stablecoin infrastructure to make meaningful improvements to their economics and processes. Leading global payments firms WorldPay and Checkout.com have integrated USDC for merchant payouts, with British company Checkout.com processing $300 million of USDC during a six month pilot.[6] Additionally, Visa, Mastercard, and a number of other traditional payments companies are already looking to stable, regulated digital currencies like USDC as an alternative settlement system. Bridging existing financial infrastructure to the modern, cutting-edge world of public blockchains will be a catalyst for trillions of dollars of economic activity. To date, USDC has facilitated the settlement of over $6 trillion dollars of transactions.[7]

The enhanced utility of USDC promotes the usefulness and attractiveness of the US dollar. Additionally, Circle's need for reliable reserve assets increases demand for U.S. sovereign debt. As of the end of 9 September 2022, Circle owned $41 billion dollars in short-dated Treasury bills, an amount greater than some prime money market funds or other international organisations. A similarly regulated, private, widely accepted pound stablecoin could generate similar benefits for the pound sterling and the United Kingdom.[8]

2. What opportunities and risks would the introduction of a Bank of England Digital Currency bring?

The development of a CBDC would be an expensive and lengthy process with unclear benefits. Indeed, this was the conclusion reached by the House of Lords Economic Affairs Committee, which said in a December 2021 report, "We have yet to hear a convincing case for why the U.K. needs a retail CBDC. While a CBDC may provide some advantages on speed of settlement and cheaper and faster cross-border payments, it would present significant challenges for financial stability and the protection of privacy." In contrast to payment stablecoins, which facilitate trillions of dollars of transactions today, the Committee also noted, "a lot of work remains to find workable solutions which do not entail difficult design trade-offs which may make a CBDC unattractive."[9]

The costs involved in creating, maintaining, and developing a Bank of England (BOE) Digital Currency - not to mention the costs associated with promotion and adoption of the U.K. CBDC in the economy - will be significant, and likely borne by the BOE and ultimately the U.K. tax payer. A digital pound would require decades-long investment in new, distinct payment channels that could withstand extreme events and nation-state-level attacks.

A Bank of England Digital Currency could also weaken anti-money laundering (AML) controls, tax compliance, and other anti-crime measures if the BOE sought to replace experienced financial institutions as the main financial intermediary in the economy. Modern financial institutions, including regulated virtual asset service providers, have spent considerable time and resources to develop sophisticated AML programs, applying advanced technology to ensure compliance. It is not clear that the BOE would be able to advance - or even replicate - these learnings if a CBDC were deployed.

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6 Worldpay from FIS® Becomes First Global Merchant Acquirer to Offer Direct USDC Settlement, Driving Digital Currency Adoption to Businesses, Team Circle, April 6, 2022 and Checkout.com becomes the first PSP to unlock weekend settlement for merchants, powered by Fireblocks' crypto payouts debut, Checkout.com, June 7, 2022.

7 Based on on-chain transactional activity (Ethereum only). View live figure at USD Coin: Crypto that's held to a higher standard, last accessed September, 2022.

8 Report of Independent Certified Public Accountants, Grant Thornton LLP, August 24, 2022 and Stablecoin issuers hold $80bn of short-dated US government debt, Scott Chipolina, *Financial Times*, August 20, 2022.

9 3rd Report of Session 2021–22 HL Paper 131, Central bank digital currencies: a solution in search of a problem? House of Lords Economic Affairs Committee, January 2022, page 43, 20.

The introduction of a Bank of England Digital Currency would also risk crowding out many of the innovative private sector solutions being developed such as privately-issued digital money that run via blockchain-based payment systems, as well as electronic and mobile money innovations. For example, USDC is used abroad by populations desperate for wealth preservation in inflationary, unstable environments. This promotes the use of the U.S. dollar abroad and opens new markets for dollar-denominated economic activity. A privately developed and operated pound payment stablecoin - adopted first in the U.K. with the endorsement of the Government and regulated by U.K. authorities - could provide similar benefits, along with the proven benefits of fast settlement, near-feeless exchange, and programmatic capability. As a leading global financial centre that has been at the forefront of digital innovation, fintech investment, and the development of digital payments, the U.K. should focus on building a regulatory environment that encourages the adoption and development of such technology, not crowding it out.

Ultimately, though, it's not clear that a CBDC could meet the constant demand for innovation from the market. Privately issued stablecoins, which compete on the open market, are likely to be more agile, tech-forward, and better-equipped. For example, Circle today natively supports USDC on nine public blockchains and is currently working on deploying USDC to other emerging chains. To fully meet the needs of users, the issuer of a U.K. CBDC would need to constantly upgrade its infrastructure and satisfy burgeoning use cases or else risk its product fading into obsolescence as the rapidly evolving world of technology opens new features, products, and services for users. Many of the purported advantages of a CBDC are already being provided by private financial institutions with a commercial incentive to keep up with user demands, including payment stablecoin issuers such as Circle.

Financial Inclusion: Serving the Underbanked and Unbanked

Additionally, it's not clear if a CBDC could improve financial inclusion given that access to a bank account would likely be required to use a U.K. CBDC. This contrasts with stablecoin-enabled, device-centric blockchain financial services that are currently expanding access to affordable, digital financial services.

FCA research highlights that more than 1.2 million U.K. adults do not have access to banking services.[10] Additionally, around 7.1 million people (around 14% of the adult population) in the U.K. fall into the definition of "financially excluded," meaning they could potentially struggle to access affordable and fair financial services.[11] Not having a bank account can impact how someone is paid their wages, pension, and social benefits. Even making payments for everyday bills is difficult as more and more cash services in councils, post offices, and neighbourhood bank branches are closing down. In addition to the logistical challenges faced by the unbanked, there is also often a price premium. The best rates for utilities, mobile phones, and insurance are reserved for those who sign up to a contract and pay by direct debit. According to a report by the U.K. fintech company Pockit, the unbanked – who are often those with the lowest incomes – end up paying an extra premium of up to £430 a year for things like electricity, gas, and loans simply because they don't have a bank account.[12] As energy prices climb, it's more important than ever to alleviate burdens placed on the most vulnerable in society.

There are many reasons that a person may be unbanked or underbanked. A person may distrust the banking system, or they may be ineligible for a bank account because they are unable to meet the ID requirements set by a bank. This latter problem has been particularly acute for victims of human trafficking, victims of domestic violence, and refugees looking to access banking services after moving to the U.K.

[10] Financial Lives 2020 survey: the impact of coronavirus, Financial Conduct Authority, November 2021.
[11] Ibid
[12] Poverty Premium Research, Bristol University, June 2022

Unlike a CBDC, stablecoins are obtainable and usable without a bank account, making them more accessible to U.K. adults. The economics of the digital assets ecosystem are fundamentally different from traditional systems and enable expanded financial inclusion. Banks make money on credit spread, collecting artificially low-cost deposits while making loans to businesses and households. Because low-balance customers don't provide deposits and the opportunity for maturity transformation, banks have no incentive to service low-income households, who are often the under and unbanked. In contrast, digital asset services are *unbundled* - the functions of custody, payment processing, and lending are separable and conducted by different actors. This reduces overhead costs and allows financial institutions to provide tailored financial services to consumers. Additional detail is provided in our response to Question 3.

Digital assets can also help increase access to safe, digital financial services precisely because many digital asset financial institutions are not banks. As stated above, many Britons may choose to be unbanked because they don't trust banks or are afraid to incur overdraft fees or take on debt they cannot afford. Today, they can access digital financial services through nonbank digital asset financial institutions. There is an incongruity in the nomenclature of financial inclusion: it is access to digital financial services that is important, not access to bank services. Circle believes that not only can unbanked and underbanked Britons still access affordable, safe, digital financial services through non-bank means, but that these populations may be *more likely* to adequately meet their needs through non-bank financial services, including those built on digital assets.

Privately-issued digital money can support robust economic activity and the conveyance of monetary policy. USDC has enabled over $6 trillion in on-blockchain payments and settlements as of 9 September 2022, and over 1.5 million active wallet addresses have conducted transactions with USDC. This data demonstrates how USDC is generating novel economic activity based on the U.S. dollar.

The private sector innovation of the past three years is an alternative path of development for the U.K. If designed and regulated appropriately, a pound-denominated, privately-issued digital currency could bring digital versions of the pound to the U.K. digital asset economy and enable payments system upgrades for all.

3. What impact could the use of cryptoassets have on social inclusion?

Financial Inclusion

In 2022, every individual should have access to digital financial services that allow them to send, secure, and receive value smoothly and inexpensively. The unfortunate reality, however, is that the traditional banking system has failed to provide these basic services to millions worldwide. The underserved also tend to be low income and/or ethnic minorities. Until recently, the under and unbanked have had to rely on money service bureaus, payday lenders, and other high-cost providers for financial services. Today, however, they can use digital assets for their financial services needs. Digital assets are advantageous because custody is unbundled from other services, they are natively digital, and open public blockchains can make unbiased, rules-based financial services decisions.

As noted above, a key innovation of public blockchain technology is that it unbundles financial services. Unbundling financial services enables competition to serve every part of a consumer's financial life, increasing choice and lowering price. In the case of digital assets custody, the most basic service required by a consumer, high-quality, free products have already emerged. Consumers today have the option to self-custody digital assets, free of charge, using personal digital wallets. Consumers simply need to remember or store a seed phrase and password paired with the wallet. This may be the right solution for some consumers who are sceptical of traditional financial services providers. Additionally, digital asset payments are increasingly available at lower cost to those offered by traditional payment service providers. Public blockchains are open and permissionless, which means anyone can read or write to the common ledger provided they pay a market-based fee to do so. This contrasts with legacy payment systems, which can only be accessed through a bank or other private financial institution. This closed, proprietary structure increases overhead costs, contributing to the structural economics that excludes many individuals from the financial system.

Gender Inclusion

The increased use of digital assets could also improve gender inclusion in the financial sector. Women face endemic financial barriers to economic freedom, access to capital fundraising, and financial independence. In the face of these challenges many are looking to cryptoassets as a way to bypass more restrictive traditional monetary systems in order to gain greater access to and control over financial opportunities for themselves, their families, and their businesses. Permissionless digital assets could enable women to access financial services independently, helping them store wealth, make frictionless payments, and invest in emerging technologies without relying on anyone else. A recent survey revealed that nearly 25% of women own cryptocurrency and 1 in 3 women stated that they plan on buying cryptocurrency in 2022.[13] Specifically in the U.K., 35% of crypto owners are women, and women make up 48% of individuals who say they will buy cryptocurrency in the future.[14]

Generational Inclusion

Additionally, the digital-first nature of the digital asset class has proven itself to be attractive to younger generations, with the FCA finding that the typical new digital assets owner is between 25 and 44 years old.[15] Learning healthy financial habits from a young age, including how young people can evaluate whether digital assets financial services are safe and beneficial, is an important skill that will improve financial wellbeing for young Britons as they mature. The Government's existing efforts to promote financial literacy among U.K. pupils, like the Money and Pensions Service's financial education guidance, includes materials that discuss cryptoassets.[16] Circle supports the U.K. government's initiatives to properly educate the next generation, and it encourages additional efforts to cultivate knowledge of digital assets among younger individuals of diverse backgrounds which will further social inclusion in the future.

Ultimately, the goal of financial products built on public blockchains is to evolve traditional financial services into alignment with the ever-growing digitisation of how people exchange value and data. Proponents of public blockchain infrastructure, including Circle, believe that unbundling financial services can lead to new and improved financial products and services. Digital assets will not replace traditional currencies but rather reduce digital finance friction, enable greater access, increase transparency, and provide consumer optionality. For

13 BlockFi Survey Reveals Nearly 1 in 3 Women Plan to Buy Crypto in 2022, BlockFi, March 2022.
14 2022 Global State of Crypto, Gemini, April 2022.
15 Research Note: cryptoasset Consumer Research 2021, Financial Conduct Authority, June 2021.
16 Robin Walker, Parliamentary Under-Secretary of State for Scotland, Minister of State (Education), They Work For You, December 2021.

example, instead of underwriting loans based on private, opaque credit scores (which leave out five million Britons[17]), smart contracts can issue loans based on verifiable cash flow and transparent, on-chain identity. Instead of routing money flows through an uncompetitive payments system, payment stablecoins move frictionlessly according to mathematical rules. The move from flawed human subjectivity - which has left millions of Britons lacking access to financial services - to rules-based transparency will increase access to basic, cheap, safe, digital financial services.

4. Are the Government and regulators suitably equipped to grasp the opportunities presented by cryptoassets, whilst at the same time mitigating against the risks?

Conflicting Messaging versus a "Whole of Government" Approach

As far back as February 2018, the House of Commons Treasury Committee initiated an inquiry into digital assets, which received 53 written submissions and hosted 3 evidence hearings (which included senior representatives from the FCA), during which the industry strenuously recommended that digital assets be regulated. The Treasury Committee's report concluded that "the FCA should be the relevant regulator for supervising anti-money laundering."[18] The parallels between then and now are considerable. Just like now, the 2018 inquiry and report succeeded a period of rapid price appreciation in cryptoassets and a surge in retail-based adoption and usage. The years after the 2017 bull market were an ideal time for the U.K. to develop a holistic regulatory regime for cryptoassets. Unfortunately, the U.K. did not act on the recommendations of the Treasury Committee. To regain its footing and status as a global financial services leader, the U.K. must act now.

Some actions taken by the Government have been positive. The Government's April announcement that it would establish the U.K. as a "global hub for cryptoasset technology and investment" was a strong statement to the world that the U.K. would vigorously defend its position as a leading financial services centre. Likewise, the Conservative government was staunchly supportive of establishing a competitive, proportional regulatory framework for the sector as part of the Government's push to make the U.K. a crypto capital. Finally, Circle was encouraged by the Government's plans to establish a cryptoasset Engagement Group to bring together key stakeholders to collaborate on issues facing the cryptoasset sector. We encourage the U.K. Treasury to ensure this forum includes leading voices from right across the sector and not just from traditional finance providers. Circle would be happy to participate.

While many recent signals from the Government have been positive and pro-innovation, some U.K. regulators have simultaneously expressed conflicting messages which have signalled that the U.K. is not a good place for digital asset development. For example, the BOE Governor called the crypto market an "opportunity for the downright criminal," and the Chair of the FCA stated that the FCA should not deign to regulate "speculative crypto tokens, which have no inherent value." Announcements to this effect discourage responsible companies from considering or remaining in the U.K., and imply a willful lack of understanding and awareness of compliant, meritorious products and services being built on public blockchains. While the Government may recognize the potential of this space - more of which is being realised everyday - there appears to be a division between the Government's intention and the appetite of regulatory authorities to implement a productive vision.

Furthermore, while the FCA's crypto sprints in May and June of this year signalled a willingness and openness to collaborate with industry participants on designing a balanced regulatory framework, it also unveiled the lack

[17] Meet the 5 million 'credit invisible' Brits still at risk of exclusion from the financial system, Experian, March 2022.
[18] House of Commons Treasury Committee cryptoassets, Twenty-Second Report of Session 2017–19, September 2018, page 33, 126-128 and page 43.

of understanding of its staff of the complex workings of the cryptoassets ecosystem. Since these were held, the FCA has failed to provide clarity on how that feedback was incorporated and set out its intended next steps.

Global Leadership Requires Qualified Regulatory Leaders

The Government should assess (and, potentially, reassess) new regulatory leaders for their "cryptoasset awareness" and consider strengthening the proposed secondary competitiveness objective to a primary competitiveness objective. Some regulatory leaders have been consistently vocal that they simply do not believe that crypto *ought* to be regulated, i.e., that it is meritless and does not deserve attention. This is no longer a viable option. Maintaining such a stance is irresponsible and leaves the U.K. at a competitive disadvantage.

If the Government intends to honour its commitment to make the U.K. a global hub for cryptoasset technology and investment, it should ensure that those leading the work around its future regulatory framework share that same vision and appetite. Circle, alongside other industry participants, has been discouraged by the lack of meaningful engagement, progress, and clarity of vision from the leaders of U.K. regulatory agencies. This has resulted in a prolonged period of regulatory uncertainty and delayed decisions which have had a negative commercial effect on innovative firms. The FCA's limited resources and apparent unwillingness to prioritise the authorisations of cryptoassets firms for AML purposes, alongside its public announcements condemning the industry, have had a negative effect on growth and competition in the market. The Treasury Committee should consider carefully the extent to which the regulators and the government are aligned and, if necessary, revisit the reforms proposed in the FSMB to ensure a strong, pro-innovation and pro-competitiveness focus as part of its Future Regulatory Framework review. From Circle's experience with the U.K. authorities, Circle believes the proposed "call-in" powers being considered by the U.K. government could be an important tool to ensure the objectives of the U.K. government are achieved, while preserving regulatory independence.

New Innovation will Require Institutional Upskilling

Unlike non-crypto fintechs, which generally build on top of the banking infrastructure that already exists, cryptoassets and public blockchains are genuinely new technological innovations that have been enabled by the combination of cryptography and the internet. Due to the flexibility afforded by the new technology, crypto entrepreneurs are rapidly building new products, services, and ecosystems. These creations often deploy novel economic, socio-political, and technological structures. They are challenging to fully understand, and the industry evolves very quickly.

Circle does not believe the Government and regulators today have demonstrated that they fully understand the opportunities presented by cryptoassets, nor how to effectively mitigate the risks. These bodies must make a conscious effort to upskill civil servants or hire staff who have deep expertise in digital assets and blockchain technology. Staff with such expertise should be knowledgeable about the basic functionality of public blockchains, the perimeter of the ecosystem, usage patterns, and how to utilise the inherent design features which enable unique risk mitigation measures which are not available within traditional finance. The Government may need to set aside additional resources, adjust pay scales, or commit to significant, substantial professional development programmes in order to upskill its workforce to the extent required. However, doing so is necessary. U.K. regulators cannot let a lack of understanding impede the business environment for crypto innovation in Britain, which in turn will harm the country's economic position. As has been deployed in other parts of financial services, Circle believes there could be benefit in a public/private partnership that can leverage the expertise of the private sector to support public agencies in developing a regulatory strategy for cryptoassets. Such an approach could be modelled on the work of the Economic Crime Strategic Board or the Cross Market Operational Resilience Group.[19] The crypto industry is global, and innovation that is unfairly stymied in the U.K.

will migrate abroad. That would be a loss for the U.K. as well as consumers who want to access new products and services that meet sincere needs.

Most policymakers remain in the "education" stage of digital asset policy. To make substantive progress on the myriad challenging issues that remain, they must be able to quickly move from understanding new products and services to considering the broader context of how such products and services fit into the greater landscape.

5. What opportunities and risks could the use of cryptoassets—including Non-Fungible Tokens—pose for individuals, the economy, and the workings of both the public and private sectors?

CRYPTOASSETS

Individuals

Cryptoassets present many opportunities for individuals to fully optimise the digital landscape to improve their lives. Specific to the fully fiat-backed digital currencies with which Circle is most familiar, the accessibility and technological improvements of blockchain-based currencies can improve personal financial health. For example, faster access to personal funds will particularly benefit those who may otherwise be limited to high-cost alternatives, such as payday loans. Many low-income consumers who take expensive payday loans have enough money to pay expenses but lack the liquidity to reconcile the exact timing of large expenses like rent with sporadic or delayed income payments.

Additionally, the borderless nature of cryptoassets is important for decreasing the cost of international remittances, a key United Nations goal.[20] Circle is working to address inefficiencies that impact traditional remittance transfers such as slow delivery and high fees for sending money across borders. Examples of Circle's work in this area include a partnership with MoneyGram International, one of the world's largest money transfer companies, which enables USDC-denominated remittances on the Stellar blockchain and facilitates cross-border payments for millions of customers worldwide. With the global reach of MoneyGram's services and the speed and low cost of transactions on Stellar, people can convert their cash into and out of USDC, giving them access to fast and affordable digital asset services that may have previously been out of reach.

One risk individuals face when engaging with cryptoassets is the prevalence of frauds and scams. The technical complexity and rapid price appreciation of some digital assets is a combination that scammers exploit. The FCA, the Advertising Standards Authority (ASA), the Joint Fraud Taskforce,[21] and the industry-led "Take Five to Stop Scams"[22] should establish additional formal opportunities to collaborate with the private sector to utilise their expertise and characteristics of digital assets to better fight scams and prevent fraud.

Additionally, consumer protection authorities should use blockchain-native solutions to prevent scams and fraud. Most digital assets are natively digital, open, and auditable, characteristics that offer advantages over traditional systems. This is most apparent in the ongoing fight against money laundering, which has benefited significantly from blockchain intelligence solutions. The same tools can be used to fight fraud and scams, and industry members have already cooperated to start addressing the fraud within the industry. Circle recently partnered with TRM Labs and others to launch Chainabuse, a user reporting tool that identifies scammers and fraudsters by on-chain address.[23] When fraud is suspected, users can check the counterparty against a public,

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19 Operational resilience of the financial sector, Bank of England, last updated: July 2022
20 UN Calls for Better Remittance Services at Lower Cost, Voice of America, June 16, 2021.
21 Joint Fraud Taskforce, U.K. Home Office, Last updated May 2022.
22 Take Five to Stop Scams website.
23 TRM Announces Launch of Chainabuse, the Multi-Chain Scam Reporting Tool that Empowers Crypto Users Against Fraud, TRM Labs, May 2022.

searchable database prior to engaging. This adds a layer of user protection using public blockchain technology's unique identifiers.

Similarly, consumer protection authorities should leverage public community investigations to identify and prevent scams. Digital assets that are natively digital, open, and auditable empower anyone in the world to investigate suspicious activity and publish findings for open source review. For example, the U.S. Department of Justice (DOJ) recently charged three individuals with conspiracy to commit wire fraud, alleging that the defendants illegally traded on insider information. The original tip[24] came from Jordan Fish, a prominent British crypto user who goes by the pseudonym Cobie, and the tip was cited by both the DOJ and Coinbase (one of the individual's employers) as an important part of the investigation. Similarly, the origin of the first U.S. insider trading case involving NFTs[25] was a tweet from a user who goes by the pseudonym 0xZuwu. The open nature of digital assets has the potential to make digital asset economies safer than traditional, closed systems.

Businesses and the Economy

Public blockchains and digital assets can reshape how the global financial and economic system operates. Payment stablecoins such as USDC are foundational to this new architecture. Public blockchains, as well as the products and services built atop them, are built to standards. These standards enable native interoperability - essentially seamless integration of new assets into existing networks. For example, a consumer may adopt an Ethereum wallet because they wish to send or receive its native token, Ether. However, USDC also operates on the Ethereum network, so the consumer can also send and receive USDC without any additional steps or software and hardware add-ons. This contrasts with the existing state of traditional payments where every asset circulates on a proprietary network. For example, a business may use faster payments to regularly send and receive money. However, when they wish to send or receive an international wire transfer they must adopt and interact with an entirely different process and counterparties.

Businesses can make use of native interoperability, near-instant settlement time, and the low transaction cost of most public blockchains to improve their processes. This is most evident for businesses that must transact internationally. Consider a company with global suppliers and clients. Today, it can use payment stablecoins for secure, low-cost, borderless international payments. Instead of having to wait days for a cross-border payment to settle, stablecoins can be used to make secure global payments that settle within minutes and cost only a fraction of the price of an international wire transfer. Additionally, because digital currencies are programmable, businesses can engage new, custom-made money flows such as programmatic mass payouts, automatic escrow, and complex trade financing arrangements - all with unprecedented levels of transparency and auditability.

Instant payments can reduce counterparty risk and assure more reliable cash flow. Today, many industries suffer from long delays in settlement that stem from out-of-sync international payments systems, communication breakdowns, and other challenges.[26] Delays in payments, and the cottage industry of business financing that compensates for the bloated system, clog up the supply chain and increase the cost of goods for end consumers. To the extent that borrowing is payment for liquidity, faster settlement structurally decreases the cost of doing business as businesses no longer need to bridge short term cash flow disruptions.

Technical complexity and a recalibration of risk assessment are probably the greatest risk of widespread use of cryptoassets in the real economy. Public blockchains are technically complex, and use of cryptoassets likely requires new processes, controls, and training. Consequences for lost funds can be significant: a mistaken payment may not be refunded, and behavioural norms may be undeveloped or unenforceable.[27] Appropriate

[24] Three people charged with $1.5m of insider trading on Coinbase, Josh Marcus, The Independent, July 2022.
[25] US brings first insider trading case involving NFTs, Hannah Murphy, Financial Times, June 2022.
[26] See, e.g., Carriers and Shippers Ready for a Payments 'Overhaul', PYMNTS.com, August 25, 2022.
[27] For example, network participants may not follow the norm of "hold harmless" agreements that exist in the wire system.

tools and processes have been developed for use by early adopters of cryptoassets, but the task of establishing best practices to businesses at scale is significant. This risk could be reduced through conduct-focused regulatory measures.

Additionally, risk-sensitive industries such as banking and insurance will need to fully understand and adjust risk ratings for crypto-native business processes. This entails coming to grips with the risks *and* benefits of public blockchains. On one hand, the risk of total loss due to a bug or error may be greater than in traditional financial infrastructure. On the other hand, the transparency of public blockchains may aid risk ratings in other ways. If the British economy is to fully leverage the transformative power of public blockchains, risk-assessors must adapt to the new technical structure of blockchain-based finance.

For certain businesses, it may be appropriate to pass new legislation or regulations segregating customer funds in accounts that have priority in the event of a financial institution's insolvency. Providing for greater bankruptcy protections would be an important consumer protection and instil greater confidence in the market.

Public and Private Sector

The growth of the cryptoasset industry is an opportunity for the U.K. to advance its position as a leading hub for global financial services. Fostering responsible cryptoasset innovation in the U.K. has the potential to add thousands of jobs and billions of pounds of economic growth and foreign direct investment. Conversely, the lack of regulatory clarity in the U.K. is hampering innovation and growth, and investors and firms are making the difficult decision to leave in favour of other jurisdictions with clear rules of the road, thus luring investment and skills away from the U.K.

Digital asset companies want to build in the U.K. Research by King's College London found that in 2021, there were over 14,000 jobs advertised on LinkedIn in the crypto and blockchain industry worldwide.[28] U.K.-based firms provided almost a quarter of those job advertisements even though the U.K. housed less than 7% of all blockchain and crypto firms worldwide. Blockchain hubs also exist in Leeds, Bristol, Cambridge, Glasgow, Belfast, Birmingham, Liverpool, and Manchester.[29] Digital asset companies want to base themselves in the U.K. and access British talent, but they will move to the E.U. or U.S. if the door is shut to them or if regulatory clarity is uncertain.

It's not just the digital asset companies who have concerns about the state of innovation in the U.K.. British leaders likewise believe the U.K. is squandering what the City of London and HM Treasury called a "once-in-a-generation opportunity to become more nimble, agile, and proportionate." The Review of U.K. Fintech led by Ron Kalifa, OBE[30] called for the U.K. to act quickly on cryptoasset policies to preserve its leading position, stating, "[t]he U.K. should aim to be at least as broad in ambition as MiCA –but should also consider whether it can develop a bespoke regime that is more innovation-driven."[31] Such a regime "should adopt a functional and technology-neutral approach… as well as the concept of 'same risk, same regulation'." As the Chairman of Network International and former CEO of Worldpay Group, Sir Ron Kalifa's perspective is astute, informed, and prescient. Circle agrees with his conclusions, including the following: "many crypto providers would positively welcome the opportunity to be regulated. Consumers are also likely to benefit if crypto firms become subject to enforceable regulatory standards."

See Finality does not exist in payments, Patrick McKenzie, Bits About Money, February 15, 2022. At the same time, norms are simply norms - they may not be enforceable in the traditional payments system, either. See, e.g., Citigroup urges appeals court to hit 'rewind' after Revlon blunder, Jonathan Stempel, Reuters, September 29, 2021.

[28] Expertise in the Crypto and Blockchain Industries: What Are the Challenges?, Alex Preda, Julie Valk, Ruowen Xu, Zining Wang, King's Business School, King's College London, Future of Work Centre, January 2022.

[29] Comptia U.K. Tech Town Index 2020, December 2020.

[30] The Kalifa Review of U.K. Fintech, Ron Kalifa OBE, February 2021

[31] Ibid, page 30.

Post Brexit, the U.K. is uniquely positioned to establish a bespoke regulatory approach that differentiates the U.K. from the E.U. and attracts leading market participants, job creation, and economic growth. In addition, embracing the digital assets industry will deliver payments system upgrades and new, retail-focused forms of exchange and value creation.

The greatest risk that the public sector faces is squandering its strong position as an existing financial centre. The U.K. can embrace digital asset innovation while protecting consumers and market stability, but if it moves too slowly, growth will move abroad. Blockchains are internet-based and natively global, so there are fewer frictions for entrepreneurs to move domiciles. Government authorities must quickly build expertise in the area and establish sensible regulatory frameworks that encourage responsible innovation while safeguarding against scams, fraud, and bad actors. This Call for Evidence is a positive step.

NON-FUNGIBLE TOKENS

A non-fungible token (NFT) is a digital asset that is stored on a public blockchain. An NFT token is a unique asset in digital form that is not interchangeable with any other digital asset. Essentially, every NFT is a 'one-of-a-kind' item. NFTs currently take the form of artwork, music, or in-game assets such as unique avatars, but in the future they may be extended to any form of identifier or property, whether that be membership in a specific group, a subscription to a music service, or anything else. NFTs are a newer form of cryptoasset that has only just begun to be explored.

Individuals

NFTs provide a truly innovative way for users to record and transfer digital property rights. Because NFTs are programmable cryptoassets, they can enable new revenue models. For example, NFTs can programmatically return a royalty to the creator upon transfer on a secondary market in an exchange unknown to the creator. This enables creators to collect revenue on their work without having to actively monitor all places in which their content is being exchanged. Content creators are using NFTs to establish new streams of revenue outside of traditional power structures in their industries, such as music.[32]

However, as with any new innovation, there remain risks related to speculative activity of the assets today. Given their nascent use cases, the viable paths to assure long term value are still being developed. Additionally, legal and regulatory questions remain as to the assurances available to the purchaser of NFT's, as well as the rights and obligations of the creator.

Businesses

For business, NFTs currently offer new opportunities to deepen relationships with their customers and audiences and create new customer experiences that delight and attract. For example, Fan Tokens issued by football clubs may give the token holder the opportunity to participate in club activities, such as choosing the intro song played when the team runs on to the pitch, choosing new team uniforms, or affording special privileges on match day. In this example, the NFT holders become part of a community, to which the token issuer can incentivise continued engagement through targeted marketing, on-chain feedback, or special access benefits which increase over time.

Another developing use case for NFTs is generating Proof of Attendance Protocol (POAP) tokens. POAPs are a kind of digital sticker that can be claimed at various events, whether virtual or physical. The concept is simple: as social networks have moved online, people want to show off online as well. In the same way you might buy a postcard or a framed photo from a National Park and keep it in your study, so too can you claim a POAP for

[32] See, e.g., Royal.io

online, blockchain-based display.

The Economy

Longer term, with a bespoke regulatory framework, NFTs could enable a much larger radius for impact, effectively becoming the source of truth for property rights of all non-fungible assets (homes, cars, memberships, etc.). The design space is largely unexplored, but the concept of verifiable ownership is powerful. While NFTs are still in their nascent phases, and fragmentation across many different blockchains networks exists, the explosion in experimentation has already led to compelling use cases that have generated intense interest (evident in this Call for Evidence). To unlock NFTs' full potential, regulatory and legal harmonisation will be required, just like with all other cryptoassets.

Through Circle's suite of Application Programming Interfaces (APIs), Circle empowers creators to facilitate unique, web3-native commerce experiences through a variety of payment methods, including a number of crypto and fiat options. Our Circle Account also provides the ability for web3 creators and businesses to manage funds received from these activities in a way that seamlessly spans both traditional and crypto ecosystems.

6. How can distributed ledger technology be applied in the financial services sector?

While public blockchain technology fundamentally challenges the traditional model of intermediated financial services, it's possible for agile, forward-thinking companies to take advantage of this period of innovation to gain customers, improve products, and prepare for the future. Circle's publicly announced partnerships and the private interest it receives from traditional financial institutions demonstrates that there are many firms who understand the opportunity.

A great example of a forward-thinking company is Checkout.com, a U.K. payment processing company. Checkout.com processes card transactions for merchants and has adopted payment stablecoins for payouts to its merchants. When merchants process a card transaction with Checkout.com, the consumer's funds settle to the merchant's account hosted at Checkout.com. Normally, merchants then receive intermittent batch payouts to their bank account. However, payouts are limited by bank infrastructure and banking hours. Even though businesses desire instant liquidity and uninterrupted cash flow, they can't withdraw their funds on weekends or holidays. Using USDC, Checkout.com can now pay merchants when banks are closed. Earlier this year, Checkout.com processed $300 million of payouts during a six month trial, showing strong merchant demand for such a solution.[33]

Another forward-looking financial institution is MoneyGram International. As mentioned previously, MoneyGram, a global leader in P2P payments, has partnered with Stellar, an open-source public blockchain, to tokenise money and transfer it anywhere in the world.[34] An integration of MoneyGram International's network with the Stellar blockchain now enables cash funding and payouts in local currency for consumers facilitated through USDC, as well as near-instant backend settlement capabilities in USDC. Consumers can now go into any MoneyGram International location to either receive payouts into their digital wallets or cash-out their digital currencies to their local currency.

Finally, payments giant Visa is exploring how it can adapt to the new paradigm of stablecoin payments. In March 2020, Visa became the first major payments network to settle a transaction in USDC.[35] Visa established a path for digital currency settlement within their existing treasury infrastructure, which moves billions of dollars each day across thousands of institutions in more than 200 markets and 160 currencies. Working with

[33] Checkout.com becomes the first PSP to unlock weekend settlement for merchants, powered by Fireblocks' crypto payouts debut, Checkout.com, 7 June 2022.
[34] MoneyGram Launches Pioneering Global Crypto-to-Cash Service on the Stellar Network, PR Newswire, June 2022.
[35] Visa Becomes First Major Payments Network to Settle Transactions in USD Coin, Visa Newsroom, March 2021.

Anchorage, the first U.S. federally chartered digital asset bank, Visa launched a pilot that allows Crypto.com, a digital asset financial services company, to send USDC to Visa to settle a portion of its obligations for the Crypto.com Visa card programme.

Circle has always recognized that the proliferation of public blockchain technology is a decades-long project. It has positioned itself as the bridge between the traditional financial system and the world's leading public blockchains to unlock growth for businesses and investors around the world. Circle takes fiat currencies and puts them on blockchains, which pairs the technological possibilities of blockchains with the stability and trust of fiat currency. The financial services sector should recognize the growth and productivity of blockchain technology and seize the opportunity. Government authorities must likewise modernise and adapt their regulatory models to accommodate this shift.

7. What work has the Government (and its associated bodies) done to understand, prepare for and, where relevant, encourage changes that may be brought about by increased adoption of cryptoassets?

The Government's forthright engagement with the industry has been welcome. Circle has found constructive audiences with policymakers about the complex regulatory and policy issues at play. However, the Government and regulators could do better in taking a strategic, measured approach to engagement with relevant stakeholders. This would make it easier for knowledgeable actors to provide high quality information in response to inquiries, and it would lead to better policy.

For example, this Call for Evidence is a welcome opportunity for Circle to express its view on various topics related to the regulation of cryptoassets. However, it comes amidst many similar inquiries from related regulatory bodies. HM Treasury published two consultations this summer: one on "Payments Regulation and the Systemic Perimeter," published July 20th, and the other on "Managing the failure of systemic Digital Settlement Asset (including stablecoin) firms," published May 31st.[36] Finally, as of 28 July, the Law Commission of England and Wales is seeking feedback on its recommendations made in response to an inquiry by the Government.[37] Circle also expects the BOE and FCA to issue additional consultations before the end of this year. These solicitations require hundreds of staff hours to respond to and raises questions from industry about how the Government, and its agencies, will evaluate all of this information. We encourage the Government to take a holistic approach to coordination across its associated bodies to ensure cohesive and consistent regulatory and legislative proposals. The Government should utilise the Regulatory Initiatives Forum[38] to plan out upcoming regulatory inquiries and developments. Using the Forum would also provide better coordination between regulatory agencies after industry submissions are complete. This would be especially effective if use of the Forum were combined with the establishment of an effective public/private partnership board. This level of coordination can help the U.K. and innovative companies develop and execute a shared, long-term strategy that will kickstart economic growth and position the U.K. as a leader amongst its peers.

When the Government does move forward on policy, we encourage it to keep the industry abreast of developments and continue to proactively engage with industry stakeholders. As previously mentioned, this Committee initiated an inquiry into digital currencies in February 2018, in which it received 53 written submissions and hosted 3 evidence hearings. One of the key conclusions was that "the FCA should be the relevant regulator for supervising anti-money laundering."[39] Yet firms who have applied for registration have

[36] Payments Regulation and the Systemic Perimeter: Consultation and Call for Evidence, HM Treasury, 20 July 2022 and Managing the failure of systemic Digital Settlement Asset (including stablecoin) firms, HM Treasury, 31 May 2022.
[37] Law reforms proposed for digital assets, including NFTs and other crypto-tokens, Law Commission of England and Wales, 28 July 2022.
[38] Regulatory Initiatives Grid, Financial Conduct Authority, Last updated: June 2022

been constantly stymied and delayed, and the FCA has twice exceeded its statutory deadlines to approve firms. To date the FCA has only registered 36 crypto firms under its anti-money laundering remit. While Circle and the industry welcome forward movement on crypto regulation, mixed messages from regulators and lack of timely execution has strained the relationship between the Government, regulators, and industry. We urge the Government to take a strategic, unified, 'whole of government' approach toward the development of cryptoasset policy and regulation - and then follow through.

8. How might the Government's processes – for instance the tax system - adapt should cryptoassets be adopted more widely?

Digital currencies can enable the transformation of public finance and Governments around the world are exploring policy and regulatory implications of digital assets. For instance, the programmability of digital currencies could enable wholesale changes to tax functions such as embedding tax within currencies to enable assessments and payments with little intervention, reduction of errors and fraud, moving tax processes closer to real-time enabling Governments to receive tax payments faster and citizens to enjoy faster refunds, and potentially moving more of the shadow economy into the formal economy.

For example, Circle is currently working on a proof of concept with the tax practice of a global professional services network and a national tax authority to scope a pilot to facilitate employee salary payroll tax withholdings utilising USDC.

9. How effective have the regulatory measures introduced by the Government - for instance around advertising and money laundering - been in increasing consumer protection around cryptoassets?

While well-intentioned, the Government's approach to regulate cryptoassets over the past half decade has been sporadic, uncoordinated, and incomplete. Messaging from officials often conflicts, leaving the industry vacillating between expansion plans and escape hatches. Circle urges the Government to set a strategic, informed, consistent, long-term course for crypto investment and innovation in the U.K. and execute it. Because efforts so far have not followed this principle, they have been cumbersome and not as effective as they could have been - largely made up of discouraging warnings and CEO letters, disjointed or isolated policies, and attempts to "square peg, round hole" cryptoassets into unsuitable existing regulatory regimes.

The U.K. should immediately advance productive crypto regulation in three areas:

Pass payment stablecoin regulation modelled after e-money regulations

The Government's Financial Services & Markets Bill will give HM Treasury the power to bring the issuance or facilitation of the use of "digital settlement assets" (DSAs) used as a means of payment into the U.K. regulatory perimeter. Initially, the new regulatory regime is primarily intended to capture stablecoin activities where stablecoins are used as a means of payment. This will be achieved by extending the existing regulatory rules that the FCA applies to electronic money and the payments systems regulatory framework to stablecoins.

The proposed legislation and new regulatory regime should help to advance national payments infrastructure, consumer choice, and business growth. Circle encourages parliamentarians to pass this vital legislation which

[39] House of Commons Treasury Committee cryptoassets, Twenty-Second Report of Session 2017–19, September 2018, page 33, 126-128 and page 43.

should give U.K. businesses, financial services firms, and consumers clarity on how stablecoins are regulated and how they can be used.

However, in thinking about how the new powers should be used, Circle encourages HM Treasury to carefully consider a bespoke regulatory regime for payment stablecoins which acknowledges the fundamental differences in their design and architecture from traditional payment systems. For example, Circle recently responded to HM Treasury's consultation on the Government's proposed approach to managing the failure of a systemic DSA firm (the FMI SAR consultation)[40] a category that may include a stablecoin issuer such as Circle. HM Treasury proposed to handle a potential failure by way of a modified Financial Market Infrastructure Special Administration Regime (FMI SAR). Circle expressed two points: first, that elements of the existing FMI SAR could indeed serve as a guide for future, comprehensive regulation of DSA firms (the FMI SAR only covers failure scenarios); but second, that the entirety of the FMI SAR would not be an appropriate pathway to regulate a DSA firm such as Circle. Both points stem from fundamental differences between digital assets circulating on public blockchains and financial institutions net settling corporate liabilities on public payments infrastructure.

First, while Circle is encouraged that HM Treasury is taking seriously the prospect of widespread DSA adoption, the application of a modified FMI SAR to "systemic" DSA firms is premature. HM Treasury and the Bank of England should first consider whether DSA firms are understood to be "systemic" under FMI definitions and whether this definition is even possible under the current FMI framework. Indeed, application of the FMI SAR framework puts the cart before the horse because the U.K. has not yet established a dedicated stablecoin regulatory regime. While development and implementation of a modified FMI SAR could be an important part of such a regime, Circle urges HM Treasury to first focus on attracting digital asset firms, implementing basic consumer protections, and providing for the widespread use of payment stablecoins.

Second, in developing any digital assets regulation, including a modified FMI SAR framework, Circle encourages policymakers to carefully consider the fundamental differences between traditional payment flows and digital assets circulating on public blockchains. Rules built for closed consortia are not appropriate for peer-to-peer networks built with the express purpose of removing financial intermediaries prone to failure. For example, public blockchains validate transactions based on open-source cryptographic rules. When an Ethereum user pays a merchant with USDC, the transaction is broadcast directly to the network as a whole instead of being routed through a dedicated payment service provider. This differs from traditional payments networks which generally consist of proprietary software and closely related financial institutions. In the latter case, it is appropriate to supervise third-party service providers and intermediaries such as central securities depositories. For a blockchain-based DSA firm, however, such a function would be unwieldy due to the fundamental difference in network structure. To adequately supervise public blockchain payments infrastructure, it may be more appropriate and effective to review the open-source code for networks, as well as the historical performance of networks on which DSAs circulate.

Lessons for how to regulate stablecoin issuers in the unlikely event of a failure also holds lessons for how to regulate stablecoin issuers in general. Circle on its own does not function as an inter-bank payment system, CSD, or third party service provider. Numerous market participants make up a dynamic and complex ecosystem of DSA firms servicing various functions of a complete FMI architecture. Circle believes that the financial stability and consumer-facing risks of a payment stablecoin issuer may differ greatly from that of a traditional FMI. Likewise, the risks of a payment stablecoin issuer differ from other DSAs such as digital wallet providers and digital asset marketplaces.

That said, there are some similarities between DSA firms such as Circle and traditional payments infrastructure providers. Circle recommends HM Treasury consider a novel, bespoke supervisory approach, potentially

[40] Managing the failure of systemic Digital Settlement Asset (including stablecoin) firms, HM Treasury, May 2022.

modelled around the FMI SAR or Payment and E-Money Special Administration Regime (PESAR) frameworks. The PESAR (either in its entirety or in parts) may be more closely aligned to the activities related to payments firms, as it was specifically established to address the risks posed by the possible failure of payment and electronic money institutions.

The PESAR was created for situations in which the insolvency of e-money or payment firms has resulted in lengthy delays in the return of customer funds. 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 power of direction over the administrator. This is very similar to the kinds of customer concerns that would emerge from the failure of a stablecoin issuer.

Within the HMT FMI SAR consultation, the Government considers that the appropriate SAR for systemic DSAs which are not banks "will generally be" the FMI SAR, and in the event of an overlap, the FMI SAR will take precedence over the PESAR.[41] However, it fails to provide clarity on the exemptions to this application, or on the specific adjustments it intends to make to the FMI SAR to reflect the specificities of the DSA market. Indeed, HMT acknowledges the FMI SAR will "require amendments to ensure the FMI SAR can operate effectively" for non-bank DSA firms.[42] The rationale behind applying the FMI SAR rather than the PESAR appears limited to jurisdictional authority between the BOE and the FCA, rather than the specific risks posed by DSA firms and their business models.

The fact that there are *differences and similarities* between DSA firms such as Circle and traditional payments infrastructure providers is not a contradiction. Innovation builds on prior primitives. A bespoke, tailored regulatory regime is required. Once again: appropriate, activity-based regulation can protect consumers and financial infrastructure while providing benefits and improvements over existing systems.

Integrating payment stablecoins into the oversight of the U.K. central bank and the sovereign U.K. regulatory perimeter would protect the public and increase payments competition. If so integrated, the Government should affirm the digital legal tender status of privately issued, regulated electronic money and digital currencies when the underlying reserve assets are in the care, custody, and control of the U.K. regulated banking system (or, ideally, held with the BoE directly).

Streamline the FCA AML registration regime

It is important that regulators such as the FCA have a clear and consistent approach to digital asset oversight which provides business certainty. The industry has raised concerns that the assessment criteria for registration applications do not follow a published or consistent methodology, resulting in arbitrary and capricious decision making.

The FCA has faced continued scrutiny over the implementation and execution of its AML registration regime for U.K. crypto firms. In February 2022, *The Block* reported that 96 firms were still awaiting a decision on their application to the FCA just weeks before a critical deadline.[43]The uncertainty forced firms to craft a "Plan B," including leaving the U.K. with no plans to return. This occurred even after the FCA twice extended the original statutory deadline to review and approve applications.

To date, the FCA has registered only 36 crypto firms under its AML remit. In April 2022, the CEO of the FCA

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[41] Ibid, page 4, 2.5.
[42] Ibid, page 3.
[43] Crypto firms face cliff-edge in U.K. as time ticks down for AML approval, Lucy Harley-McKeown, The Block, February 2022.

Nikhil Rathi defended the FCA's tough stance on crypto, declaring "clear lines" are required for the industry. Circle agrees, and it further agrees with Mr. Rathi's statement that firms must comply with "basic expected standards." Yet firms that have tried to comply by applying under the FCA's registration regime are not being processed.

Implement clear and workable guidance for financial promotions

HM Treasury has confirmed that it intends to bring "qualifying cryptoassets" within the scope of the U.K.'s financial promotion regime. This definition excludes electronic money, certain payment tokens, and central bank money but would include most cryptoassets traded on retail exchanges such as Bitcoin and Ether. Circle agrees that guidelines for financial promotions are needed for cryptoassets.

Circle strongly supports the principle of ensuring that crypto financial promotions are fair, clear, and not misleading. Financial promotions should be effectively regulated and robustly enforced. This is essential to building consumer trust, protecting consumers, ensuring consistent standards, and stamping out irresponsible practices. However, the FCA's proposed "FSMA s21 approver" rules are onerous, not proportionate to the rules for other industries, and will create an unlevel playing field that negatively impacts smaller firms.

The FCA recently proposed to amend the Financial Promotions Order to require firms to have their financial promotions approved by an FSMA-regulated firm under "FSMA s21 approver" rules. But without changes, this would prevent the majority of responsible cryptoasset firms in the U.K. from approving their own financial promotions, even if clearly compliant. This is because any firm that does not hold Part 4A permissions under the Financial Services and Markets Act (2000) cannot approve its own financial promotions. Given that the majority of crypto firms in the U.K. do not have (and do not require) Part 4A FSMA permissions, the practical effect will mean all crypto firms in the U.K are forced to seek approval from a third-party approver, at a time when there is not sufficient capacity in this market to do so. The ultimate impact will be a de facto ban on crypto advertising, which will significantly hamper the ability of firms to operate in the U.K.

The problem is further exacerbated by the fact that crypto firms in the U.K. are often unable to find suitable (in terms of knowledge, expertise, and a lack of conflicts) third-party approvers for their financial promotions. The range of firms who both possess Part 4A permissions and can also satisfy the competence and expertise requirements is extremely limited. The FCA itself has acknowledged the dearth of suitable third-party approvers.[44]

These challenges are compounded by the FCA's intention to provide a very limited transitional period for firms to comply with the new requirements. The changes required by the crypto industry are significant, and the business operations of firms will be severely impacted. Rapid adoption of the rules, especially without addressing the issues identified above, would leave the U.K. crypto industry at a significant disadvantage compared to other jurisdictions, including the E.U.

Over the past year, the ASA has, without clear guidance, issued enforcement actions against crypto companies' advertising. Many of these enforcement actions were executed without clear prior guidance from the ASA. In explaining the reasoning behind the actions, the ASA has applied inconsistent standards and cited unspecified "complaints" as the reason for concern. Industry has interpreted this erratic enforcement regime as amounting to essentially a shadow ban on crypto advertising. Additionally, the ASA is a non-statutory organisation and so cannot interpret or enforce legislation. They receive their remit over regulated and non-regulated financial promotions in broadcast advertising under a Memorandum of Understanding with the FCA.

Circle supports regulation of financial promotions related to cryptoassets. However, the current regime as

[44] Strengthening our financial promotion rules for high risk investments, including cryptoassets, Consultation Paper CP22/2***, Financial Conduct Authority, January 2022, page 43, 5.36-5.39.

proposed is unworkable and unsustainable. We would encourage the FCA, along with the ASA, to provide clear, measurable, and practicable guidance for advertising language used by the crypto industry. This could be supported by the development of consistent standards through which crypto firms can educate consumers about new products and services, promote opportunities for consumers, and comply with the law. Guidance should be as detailed and even-handed as that which is issued for fintechs, banks, and other traditional financial institutions.

10. Is the Government striking the right balance between regulating cryptoassets to provide adequate protection for consumers and businesses and not stifling innovation?

The U.K. has a history of stewarding financial innovation and attracting global talent and investment. To ensure that it continues to lead globally, it should establish activity-based, technology-neutral regulation. Additionally, it should take care to distinguish different classes of digital assets based on their economic behaviour rather than combining disparate innovations into one basket. To date, the U.K.'s approach to regulating digital assets has appeared disorganised, which has created uncertainty for both regulators and market actors. Ultimately, the result is middling performance in both aspects: U.K. regulation does not fully protect consumers and businesses because regulation is haphazard or pushes firms offshore (where they can still serve U.K. residents with unregulated services). Simultaneously, the lack of regulatory clarity inhibits long term investment, stifles innovation, and leaves consumers vulnerable.

This could not come at a worse time: Europe recently agreed upon the holistic, region-wide Markets in cryptoasset regulation (MiCA), and the U.K. is at risk of losing real economic activity to its neighbouring economic market. Already, companies have left the U.K. for other countries where the regulatory climate is welcoming and authorities provide the clarity needed for long term investment, such as France.

To be globally competitive, the U.K. must undertake the difficult task of reckoning with what is novel about cryptoassets while also understanding what risks are similar to those in existing financial services. Today, U.K. regulators do not do this, instead attempting to smush cryptoasset activities and firms into existing regulatory frameworks that are poorly suited to address cryptoasset-specific risks. Simultaneously, the legacy frameworks cannot leverage and unlock the unique benefits of cryptoassets. Cryptocurrencies and public blockchains are *genuinely new* technologies enabled by applying the combination of public key cryptography and the internet to financial assets. Regulatory frameworks based on fundamentally different technologies will not be effective.

In many other ways, the activities of some cryptoasset firms are very similar to those of traditional firms. For example, some firms issue loans denominated in cryptoassets. This is not a contradiction - the cryptoasset space is large, diverse, and growing. Instead, it identifies the need for a bespoke, tailored regulatory regime that brings cryptoasset firms to the same level of risk as traditional firms without shedding the gains that have been made. In cases in which an activity is fundamentally similar to existing activities - for example, money transmission, e-money issuance, or financial markets infrastructure construction - prudential rules can be adapted and adopted. When this happens, the U.K. can expect that a cryptoasset financial institution should conform with all appropriate obligations. But likewise, the financial institution ought to receive the same privileges, benefits and access to services, such as banking facilities and insurance, afforded to traditional financial institutions.

11. Could regulation benefit cryptoasset start-ups by improving consumer trust and resilience?

Circle has a keen interest in the development of a transparent and well-regulated digital assets market that facilitates capital formation, maintains fair, orderly and efficient transactions, and protects consumers.

Partnership between the public and private sector is critical in developing technology-neutral, principled, activity-based regulation. Circle has always taken the position that government regulation is essential to the prospering of public blockchain technology. Since its founding, Circle has prioritised responsible financial services innovation and constructive engagement with regulators and public authorities around the world. Circle CEO Jeremy Allaire testified at the first congressional hearing about cryptocurrencies in 2013,[45] and he recently testified again in December 2021.[46]

From Circle's perspective, it's unquestionable that sensible regulation that recognises the benefits, risks, and idiosyncrasies of cryptoassets and public blockchains would improve consumer trust and resilience. In many ways, financial services built on public blockchains are safer than traditional products. For example, many projects are open source, and flows into and out of protocols are visible on-chain (for example, every mint and burn of USDC is visible on-chain, and various unaffiliated websites[47] track various USDC metrics). However, consumers should not be expected to examine source code or on-chain data prior to engaging with financial services. Instead, consumers should be able to have confidence that there is a regulatory scheme in place that will protect them against egregious and harmful practices.

As cryptoassets, digital currencies, and public blockchains have developed over the past decade, entrepreneurs in this space have built a $1 trillion sector. Both industry and policymakers have learned lessons and increased understanding of how to responsibly harness these innovations. Circle encourages the U.K. government to espouse and practice activity-based, technology-neutral regulation. This will enable consumers to use cryptoasset innovations with confidence and empower the U.K. to lead in this new economy.

12. How are Governments and regulators in other countries approaching cryptoassets, and what lessons can the U.K. learn from overseas?

Cryptoassets are fundamentally global, and the U.K. must work with other nation states to harmonise regulatory frameworks. Simultaneously, though, the U.K. would benefit economically by competing with other countries to attract and onboard responsible digital asset companies. A balanced and holistic regulatory regime for cryptoasset products and services, including the issuance of payment stablecoins, would make the U.K. an attractive place to do cryptoasset business. We encourage U.K. policymakers to seek a proportionate approach that appropriately mitigates risk without stifling innovation.

The United States is leaning into the competitive advantage it already has in the payment stablecoin market. In March 2022, President Joe Biden signed an Executive Order on Ensuring Responsible Development of Digital Assets. The order activated agencies from across the federal government - beyond simply financial regulators - to consider the role digital assets would play in the United States' future economic competitiveness and national security. The Executive Order sent a strong signal to the crypto industry that the President and his government are taking seriously the innovation and growth already underway - and their implications going forward. As a senior administration official put it when announcing the order, "Ensuring responsible innovation and evolution of the digital asset ecosystem is essential to our national security, financial stability, economic competitiveness, and continued global leadership."[48]

U.S. efforts go past the exploratory stage. Powerful policymakers including congressional leaders and Treasury

[45] Key Senate Committee Holds First Congressional Hearing on Virtual Currencies, November 2013.
[46] Written Statement of Jeremy Allaire, Co-Founder, Chairman and CEO of Circle Before the House Financial Services Committee, December 2021.
[47] See usdc.cool | The USDC stablecoin supply scanner or USDC | stablecoins.wtf.
[48] Background Press Call by Senior Administration Officials on the President's New Digital Assets Executive Order, The White House, 9 March 2022.

Secretary Janet Yellen and the President's Working Group on Financial Markets have introduced or called for legislation that would create a bespoke regulatory model for the issuance of payment stablecoins.[49] For example, legislation drafted by Senator Pat Toomey, the leading Republican Senator on the Senate Banking Committee, would create a new federal licence for payment stablecoin issuers and would bring registered issuers under the supervision and regulation of federal financial regulators.[50] Likewise, Treasury Secretary Yellen recently convened a special session of the Financial Stability Oversight Council to underscore the "urgent need" to regulate stablecoins and encouraged financial regulators to "constructively engage in serious legislative efforts" to do so.[51] Leading U.S. policymakers recognize the unique benefits and risks of payment stablecoins for the U.S. economy, and they are making an active effort to establish a sensible federal framework for stablecoin issuance.

Prior to these recent federal efforts, individual states in the U.S. have created regulatory clarity for digital assets. One of the clearest examples of this is the New York Department of Financial Services' (NYDFS) June 2022 regulatory guidance on U.S. dollar-backed stablecoins. The guidance established an easy-to-follow, bright-line rule: payment stablecoins must be fully backed by reserve assets held at regulated financial institutions and be subject to regular, independent attestations.[52] This type of regulatory guidance conveys NYDFS's expectations. Regulatory clarity reduces barriers to entry because start-ups don't have to build out multi-million dollar legal operations to sort through conflicting, overlapping, and ambiguous regulations.

The European Union has also made significant progress in establishing a new regulatory framework tailored to digital assets innovation. Earlier this summer, the European Parliament adopted the Markets in Cryptoassets Framework (MiCA), which will be to cryptoassets what General Data Protection Regulation (GDPR) was to privacy (both the good and the bad). MiCA is a comprehensive framework for regulating various parts of the crypto industry including payment stablecoin issuers, the prevention of money laundering, and crypto intermediaries. Circle encourages the U.K. to review MiCA carefully. There are areas in which the U.K. should harmonise its standards with those of MiCA, for instance, standards for certain types of cryptoasset activities such as custody. Simultaneously, there are opportunities for U.K. leadership to capitalise on the regulatory flexibility afforded it post-Brexit, for example in the areas of unnecessary capital buffer requirements for fully reserved payment stablecoin issuers and transaction caps. These misguided regulations will only serve to limit consumer optionality and cut off Europe from the global flow of digital asset liquidity (and stability), and they should not be repeated in the U.K.

Japanese regulators and companies have also advanced efforts to have and enforce responsible market conduct. Earlier this year, the National Diet passed a bill clarifying the legal status of stablecoins. Like the NYDFS guidance, it clarified standards for issuers of stablecoins and laid out clear requirements for permissible stablecoin constructions.[53]This was much-needed clarity that will help businesses serve Japanese customers in a

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[49] President's Working Group on Financial Markets Releases Report and Recommendations on Stablecoins, U.S. Department of the Treasury, November 2021.

[50] Toomey Announces Legislation to Create Responsible Regulatory Framework for Stablecoins, U.S. Senate Committee on Banking, Housing, and Urban Development Minority, 6 April 2022.

[51] READOUT: Secretary of the Treasury Janet L. Yellen's Meeting with the President's Working Group on Financial Markets, the OCC, FDIC and CFPB on Stablecoins, U.S. Department of the Treasury, 30 June 2022.

[52] Superintendent Adrienne A. Harris Announces New DFS Regulatory Guidance on the Issuance of U.S. Dollar-Backed Stablecoins, New York Department of Financial Services, June 2022. Circle's audited financial information can be found as part of its public filings with the U.S. Securities and Exchange Commission (navigate to Circle's May 4th S-4/A submission, "Index to Financial Statements," page F-1). Circle also voluntarily publishes monthly accountant attestations specific to the USDC reserve and weekly data about USDC issuance and redemptions on the main information page for USDC. For a description of the difference and appropriateness of accountant audits versus attestations, see How to Build Trust, Jeremy Fox-Geen, 3 June 2022.

[53] Japan Passes Stablecoin Bill That Enshrines Investor Protection, Taiga Uranaka and YU.K.i Hagiwara, Bloomberg, 2 June 2022.

safe way.

There are opportunities for the U.K. to lead in the cryptoasset industry, but they are rapidly closing. Global leaders such as the United States, the E.U., and Japan are advancing bespoke, well-tailored regulatory frameworks for their cryptoasset industries and leaning into industry growth. The U.K. has a narrow window in which it can retain its legacy as a financial innovation centre. Otherwise, it will find itself displaced by more forward-thinking jurisdictions.

13. The environmental and resource intensity of using cryptoasset technology.

Like any industrial activity, public blockchains require energy to function. The energy is generally used to secure blockchain networks against attack, preserving wealth stored on blockchains (approximately $1 trillion as of 30 August 2022) and processing transactions. The volume of energy required to secure a network is determined by the network's specific consensus mechanism: the Bitcoin network uses the Proof-of-Work consensus mechanism, which has benefits and costs. In 2020, it was estimated that proof-of-work used 247 terawatts of power, which is about 0.16% of global energy consumption.[54]However, most networks today either use, or are soon transitioning to, less energy-intensive consensus mechanisms such as Proof-of-Stake.

Eliminating proof-of-work mining would not put a meaningful dent in carbon emissions and may slow progress in transitioning to more renewable energy production and usage. Transitioning to greener energy sources requires significant investment in new energy technology from industries that are committed to working with policymakers and the energy industry. Proof-of-work miners serve as reliable base customers who provide consistent demand – and revenue – for utilities to build out clean energy infrastructure. For grids that rely on intermittent renewable sources such as wind power, Bitcoin mining can provide the base load required to build out mass renewable instalments while powering down when demand rises.[55]

The unique characteristics of Bitcoin mining could have positive effects for environmental grids trying to decarbonise, such as that of the U.K. They can power down to redeploy critical use of power elsewhere, almost instantly, something other high-demand industries simply cannot do. The power being used by proof-of-work miners flows back to the grid giving retail consumers extra capacity in mere minutes with no adverse effects. No other industry that uses similar levels of energy, including data centres, cloud service providers, and manufacturing facilities, has the ability to do this.

Many cryptoasset companies already undertake significant efforts to be environmentally conscious. The Bitcoin Mining Council, a consortium of Bitcoin miners primarily located in Europe and North America, reported that 59.5% of the energy used by its members in Q2 2022 came from sustainable sources (including nuclear).[56] For reference, the U.K. generated 43% of its energy from renewable sources in 2021.[57]

This sustainability impact will only continue to grow over time as digital asset miners form partnerships with energy providers, utilities, communities, and other groups to develop new base energy demand. This demand provides new and valuable economic incentives for energy companies to build green infrastructure and sources of power, and it pays dividends to local communities by creating jobs and increasing tax revenue.

Circle supports USDC on nine blockchains. All blockchains Circle supports either employ the less energy-

[54] Global Bitcoin Mining Data Review Q1 2022, Bitcoin Mining Council, March 2022, page 5.
[55] See RFI Response: Climate Implications of Digital Assets, Bitcoin Policy Institute, last accessed 30 August 2022.
[56] Q2 Bitcoin Mining Council Survey Confirms Year on Year Improvements in Sustainable Power Mix and Technological Efficiency, Bitcoin Mining Council, 19 July 2022.
[57] U.K. targets power from 100% renewable sources by 2035, S&P Global Commodities Insights, 4 October 2021.

intensive Proof-of-Stake consensus mechanism or have plans to imminently do so (in the case of Ethereum). Circle believes it is important for all actors in the cryptoasset space to be conscious of their energy use as ethical corporate actors, and encourages the U.K. to consider ways to incentivise cryptoasset companies, along with all industries, to reduce their carbon footprint.

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CONCLUSION

Circle appreciates the opportunity to provide our comments into this important inquiry. We look forward to working constructively with the Committee and Government in the development of new legislation and regulations for the stablecoin and cryptoasset sector. We would welcome the opportunity to engage in future discussions and would be happy to answer any questions the committee may have regarding the evidence submitted.

November 2022