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Dear Matthias,

DP 17/3 Discussion Paper on distributed ledger technology

This is the Financial Services Consumer Panel's response to DP 17/3 Discussion Paper on Distributed Ledger Technology (DLT).

The Panel welcomes the FCA's engagement on this topic. It is important that the FCA keeps abreast of rapidly developing technology, such as DLT, so that its potential is harnessed to deliver better outcomes for consumers, whilst also ensuring the regulatory framework delivers appropriate consumer protection.

We commend the FCA's clear and accessible explanation of a relatively complex subject. This helps commentators who are not close to the technological advances but who wish to make sure that the consumer voice is heard. However, it is not clear to the Panel that DLT offers compelling consumer benefits at this stage.

Much of the Discussion Paper deals with the technical details of DLT, or potential use cases, and poses questions to firms. We have not responded to the questions but make a number of broader points that the Panel would like the FCA to take into account as it progresses this area of work:

- **Governance and liability** – Since DLT is a shared system, there is no single owner. This means that regulators should ensure that governance arrangements are adequate, and liability is clear, so that end users in a distributed system are informed and protected. We would welcome clarification on how the impact on end users would be managed and mitigated if these factors are not adequately addressed.
- **Security and resilience** – DLT is a combination of existing technology types, and so it is likely to present similar challenges and risks as technology in use today, as well as ushering in new risks. Longstanding concerns about the security, resilience and integrity of critical systems will be equally applicable to DLT. The Panel encourages the FCA to consider the security and resilience of DLTs, how assurances can be provided about the robustness of systems, including their ability to withstand cyber-attacks, as well as what should occur if they suffer a severe outage. While the distributed nature of DLT should offer a degree of protection against catastrophic systemic failures, a system-wide failure is nevertheless possible (e.g. by the dissemination of an error in code throughout the network) and so the FCA must consider how protection can be achieved and systems recovered.

- **Smart contracts** – We note that DLT can foster greater levels of automation through smart contracts. While the Discussion Paper details some potential use cases (e.g. in payments and insurance), we are concerned that their use could cause consumer harm. For example, smart contracts may not adequately reflect the practical and legal complexity inherent in insurance contracts, with the consequence that consumers may not be properly covered, or may find that subsequent claims are not valid. In addition, there would be the risks of potential consumer harm if smart contracts were to be aggressively pursued, with no recourse to human appeal. The FCA should be alive to this risk and ensure that if smart contracts are introduced then they should be implemented in a way that is sensible, and which provides the opportunity to deal flexibly with issues which may require human intervention.
- **Interaction with data protection rules** – The complexity involved in amending or removing data entries in DLTs raises questions about its alignment to provisions in the GDPR, in particular the right to erasure (also referred to as the right to be forgotten). The Panel agrees with the recommendation made in the Discussion Paper that firms should consider guidance from the Information Commissioner’s Office (ICO) on this matter where DLT is used to store, share and process client data.
- **Digital currencies** - The Panel has concerns about digital currencies, which are unregulated and volatile, and whether consumers understand these risks. Simply putting warnings on the FCA’s website is not an adequate response. The FCA should also consider how it could disseminate risk messages more widely.

Yours sincerely,

Sue Lewis
Chair, Financial Services Consumer Panel