FCA
Financial Services Consumer Panel

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Dear FCA,

The Financial Services Consumer Panel[1] welcomes the opportunity to respond to the FCA's Consultation Paper on Progressing Fund Tokenisation.

The FCA's approach to innovation and technology in asset management, as outlined in DP23/2 and expanded in CP25/28, marks a strategic shift towards modernising the UK's regulatory framework to accommodate emerging technologies such as fund tokenisation and digital engagement tools.

The Panel agrees that technology is driving significant changes in consumer expectations. With 47% of neo-broker users aged 18–34, compared with 49% of traditional investment platform users aged 55 and above[2], there is a clear generational divide and growing appetite among consumers for low-cost and direct (fractional) investments.

Furthermore, FCA's research published in December 2024 revealed that 66% of young investors make investment decisions within 24 hours[3], with 14% finalising choices in under an hour. This impulsive behaviour, often driven by social media and FOMO, signals a need for clearer disclosures and more intuitive product frameworks, a central theme of the FCA's CP24/30 consultation[4]. The growing popularity of exchange-traded funds (ETFs) among younger investors[5], who are 80% more likely to hold ETFs than older age groups, further highlights their preference for flexible, real-time trading options. These insights reinforce the importance of

[1] https://www.fca.org.uk/panels/consumer-panel
[2] https://www.fca.org.uk/financial-lives/financial-lives-2024
[3] FCA finds two-thirds of young investors take less than 24 hours to make investment decisions | FCA
[4] FCA finds two-thirds of young investors take less than 24 hours to make investment decisions | FCA
[5] UK investor insights & trends | BlackRock

designing investment platforms that meet the expectations of digitally native consumers.

The Panel recognises that fund tokenisation has the potential to:

- streamline operations by enhancing efficiency and reducing settlement times;
- reduce costs;
- enable new forms of investor engagement through fractional ownership and broader retail participation;
- enhance transparency and traceability; and
- position the UK as a global hub for digital asset management.

With that in mind, the Panel emphasises the importance of establishing a clear and robust framework for tokenised funds—one that ensures consumers are adequately protected and that innovation does not compromise investor safeguards. The Panel believes that rules must evolve with emerging technologies, and that regulatory changes should continue to prioritise consumer interests, particularly around conflicts of interest and product suitability. Disclosures must also be rigorously tested to prevent misleading perceptions.

The Panel considers that the introduction of tokenised units within authorised funds presents a range of risks that must be appropriately mitigated before such products can deliver genuine benefits to consumers. A key concern is that token holders may not enjoy equivalent rights and protections to those of traditional investors, potentially leading to an uneven playing field.

The Panel also draws attention to the potential for principal–agent conflicts between token holders, non-tokenised unit holders, and fund managers. Where funds are issued in both tokenised and traditional forms, questions arise as to whether token holders would possess equivalent rights in the event of an issue. Furthermore, if tokenised funds are initially deployed within wholesale markets and held by large intermediary unit holders, the FCA should consider whether retail investors in traditional units could be placed at a material disadvantage.

To avoid regulatory inconsistency, the Panel believes the framework should clearly define tokenised units as investments. This would ensure that equivalent risks give rise to equivalent regulatory outcomes, minimising the potential for regulatory arbitrage.

Comprehensive safeguards are also needed to protect investors from fraud, cyberattacks, and the loss of access credentials, and to ensure

assets can be transferred to heirs following the death of a token holder. The Panel encourages the FCA to clarify how digital registers will be maintained to ensure consumer protection, in particular:

- How will digital registers be safeguarded against fraud and hacking?
- What mechanisms will enable investors to regain access to assets in the event of lost passwords or access credentials?
- What procedures will ensure heirs can claim assets once probate has been granted?

In conclusion, while the FCA's Consultation Paper provides valuable clarity, it also highlights several areas where consumer protection, operational resilience, and legal certainty require strengthening. The Panel's key recommendations include:

- Expanding technical guidance to ensure consumer rights, transparency, and recourse are equivalent to traditional systems.
- Addressing operational risks such as cloud dependency, private key control, and interoperability challenges.
- Mandating smart contract audits, insurance or compensation schemes, and clear liability allocation to protect consumers from technical failures and errors.
- Introducing robust onboarding, human oversight, and rapid remediation processes to address eligibility and operational errors.
- Requiring clear, plain-language disclosures and standardised communication to enhance investor understanding and confidence.
- Supporting interoperable token standards, privacy safeguards, and contingency planning for network outages.
- Endorsing a phased, pilot-based approach to implementing direct dealing and T+1 settlement, underpinned by comprehensive risk assessments and consumer safeguards.
- Supporting prudent risk management measures, such as maintaining bank exposure limits and daily cash reconciliations, to protect investors' capital.
- Ensuring ongoing regulatory oversight, clear accountability, and robust client money protections within new operating models.

Overall, the Panel commends the FCA's efforts to enhance consumer protection, market integrity, and international alignment in this rapidly evolving sector. It supports the overall direction of the FCA's proposals but emphasises the need for tailored, enforceable rules that reflect the unique risks and dynamics of tokenised funds.

The Panel believes that the FCA's priorities for work on tokenised funds should be determined by the potential benefits to consumers. These include reduced costs, a more navigable system, stronger safeguards against conflicts of interest, and improved access to information that supports better decision-making.

The Panel's responses to the questions posed in the Consultation Paper are set out in Annex A below. The Panel appreciates the FCA's continued efforts in this area and looks forward to further engagement on these important topics.

Yours sincerely,

Chris Pond

Chair, Financial Services Consumer Panel

Chapter 2 – Accelerating tokenisation of authorised funds- now – COB Wednesday 5 November

Authority of Manager

1 Does the proposed guidance provide adequate clarity on how firms can use DLT to support the operation of fund registers?

While the proposed guidance provides some clarity on how firms can use Distributed Ledger Technology (DLT) to support the operation of fund registers, it does not go far enough in addressing the consumer protection implications. Consumers need:

- assurances that their rights are equivalent to those under conventional systems;
- transparency about who can alter, access, and correct on-chain records; and
- explicit guarantees of recourse in the event of system failure, error, or fraud.

Although the FCA outlines that managers may retain authority through private keys or "masternode" control, these technical mechanisms may not provide consumers with clear or comprehensible assurances of protection. From a consumer perspective, such arrangements could appear opaque and may not sufficiently demonstrate accountability or reversibility in practice.

The Panel therefore recommends that the FCA expand its technical guidance to include explicit reference to the consumer implications of DLT-based register operations. This should cover how firms will uphold consumer rights, ensure accuracy and data integrity, and provide accessible routes for correction and redress. Clear, plain-language safeguards are essential to ensure consumers can trust that tokenised fund registers offer the same level of protection, transparency, and recourse as traditional systems.

2 Are there any challenges in meeting the current requirements where DLT platforms are used, or in respect of emerging use-cases?

There are several challenges in meeting current regulatory requirements where DLT platforms are used, particularly in emerging use cases. These challenges relate to system resilience, governance, and operational integrity, all of which have direct implications for consumer trust and market stability.

Single Point of Failure

- Cloud Dependency - Cloud Outage on Tokenised Funds

Despite the decentralisation ethos of blockchain, many tokenised funds still rely heavily on centralised cloud providers such as AWS for critical operations. When cloud systems fail[6], tokenised funds can experience serious disruptions. During the recent AWS outage, users of major platforms such as Coinbase and Robinhood were locked out for hours, unable to access their accounts, execute trades, or view holdings. Similar risks apply to tokenised fund systems that depend on cloud infrastructure. When cloud services hosting smart contracts become unavailable, automated functions such as subscriptions, redemptions, or NAV updates can stall, potentially leading to pricing errors, transaction failures, or delayed settlements. If reconciliation processes rely on cloud-hosted APIs, outages may create inconsistencies in fund records. In addition, fund administrators, custodians, and compliance teams that depend on cloud systems may be unable to perform key regulatory or operational functions.

From a consumer perspective, such outages can significantly erode trust—particularly where investors experience financial loss due to missed trades or delayed redemptions. The UK Parliament has already begun to question whether major providers like AWS should be regulated as "Critical Third Parties" due to their systemic importance to financial infrastructure[7]

- Private Key Control Risks

If the firm managing the register also controls the private keys, this creates a single point of failure. Loss, theft, or misuse of those keys could compromise the entire register, including ownership records and transaction histories. This risk challenges the core principles of security and trust that DLT aims to enhance and raises important questions about accountability and recovery mechanisms.

Operational Complexity and Fragmentation

DLT introduces new layers of operational complexity, particularly around interoperability between systems. Without common standards, firms risk

[6] Crypto traders locked out as AWS outage cripples Coinbase and Robinhood - CoinJournal
[7] https://eandt.theiet.org/2025/10/21/mps-question-resilience-uk-banking-systems-after-aws-failure-hits-lloyds-and-halifax

developing isolated, non-scalable solutions that cannot integrate effectively with traditional financial infrastructure.

To address these challenges, the FCA should consider setting clearer expectations for operational resilience, cloud dependency management, and key custody governance within DLT-based fund operations. Furthermore, promoting common interoperability standards and recognising the systemic importance of critical third-party providers will be key to ensuring that tokenised funds operate safely, reliably, and in consumers' best interests.

Smart contracts and eligibility verification

3 Do our existing rules and proposed guidance provide sufficient flexibility to allow for firms operating the register to use smart contracts for the purposes above?

The FCA consultation paper recognises the potential efficiencies that DLT and tokenisation can deliver for firms; however, it provides limited clarity on how consumers will be protected when things go wrong.

Many of the proposed benefits—such as peer-to-peer transfers, automatic eligibility checks, and multi-wallet reporting—appear to shift operational responsibility onto consumers, creating several practical concerns.

For example, the text does not specify who bears the loss when a smart contract bug, erroneous whitelist, or incorrect eligibility decision results in financial detriment to consumers. It remains unclear what would happen if a bug in a transfer contract allowed tokens to be drained, or if units were incorrectly minted or revoked. This issue is particularly important where the regulator may be unable to enforce redress due to the immutability of a contract and where the manager claims to have "no authority to change on-chain state." To protect consumers in such cases, the FCA should require mandatory smart contract audits, insurance or compensation schemes, and clearly assigned legal responsibility. The Panel proposes that an insurance or compensation fund be established to protect consumers from technical failures, operational errors, and cyberattacks. The Panel also encourages the FCA to ensure that liability is clearly allocated and that accessible dispute resolution and compensation routes are available to consumers in these circumstances.

Similarly, there is no discussion of how concentration risk will be managed where a manager's platform consolidates multiple wallet holdings, potentially creating a single point of failure during operational outages or system failures.

The text also fails to provide clarity on what consumer protections or reversal mechanisms exist for immutable ledgers when accidental transfers or coding errors occur that cannot be reversed.

Ordinary investors may not fully understand complex concepts such as whitelists, blacklists, multiple wallets (hot, cold, exchange and dedicated), or on-chain records, which limits their ability to provide informed consent. The Panel believes that consumers must be provided with clear and accessible explanations of these concepts before they choose to participate.

Furthermore, there is no explanation of how consumer information will be protected on public chains where transactional histories are visible. Even pseudonymous wallets can be de-anonymised, potentially exposing consumer holdings and tax status, which increases the risk of privacy breaches and makes consumers more vulnerable to fraud.

The text does not address consumer portability or the ability to switch between platforms and token standards. It also does not explain how cases will be managed where eligible retail investors are unfairly blocked due to incorrect wallet or address details, or where KYC systems misclassify them. The current approach assumes firms will always correctly map wallets to real customers—a weak point for consumer protection. Where an investor's wallet or address is misattributed or unrecognised, transfers or redemptions may be prevented, resulting in consumers' funds being temporarily or permanently locked or incorrectly transferred.

The Panel recognises that strict eligibility automation can improve efficiency but notes that it can also disadvantage consumers in such situations. To mitigate this, the Panel recommends that firms implement robust onboarding procedures, transparent criteria for whitelists and blacklists, human oversight and intervention ("human-in-the-loop") processes, manual overrides, and rapid remediation service-level agreements (SLAs) to strengthen consumer protection and clarify custody responsibilities.

While allowing managers to report aggregated positions is helpful, the text provides no clarity on how consumers can verify that this aggregation is accurate or how mismatches will be resolved. Black lists and white lists also rely on accurately linking a real person to a wallet, yet the process for correcting false positives—such as being wrongly added to a black list or white list—is not explained.

Given these potential failure scenarios, the Panel recommends that while the FCA should maintain flexibility for firms operating the register, it should also introduce binding requirements—or strong

supervisory expectations—around auditability, liability, disclosure, remediation, and privacy. The Panel recommends that the FCA requires firms to demonstrate, before live deployment, how consumers would be protected in each of the common failure scenarios outlined above.

4 What role can regulators play in supporting the development of token standards that promote effective governance and positive consumer outcomes?

Regulators should take an active, enabling, and supervisory role by:

- Establishing clear regulatory expectations and standards. The FCA should set technical and governance requirements for firms, including independent smart contract audits, clear liability allocation, disclosure and remediation processes, privacy safeguards, and continuous monitoring and reporting.
- Encouraging insurance and compensation mechanisms to protect consumers from losses caused by technical failures, operational errors, or cyberattacks.
- Setting clear rules on liability, complaints handling, and compensation schemes to ensure accountability, redress, and reversibility in cases of smart contract bugs, misattribution, or system errors.
- Embedding accessible dispute resolution processes within the operational design of tokenised systems, ensuring consumers have clear routes to raise complaints and obtain compensation.
- Requiring "human-in-the-loop" controls within automated eligibility and transfer systems to address errors such as incorrect whitelisting or misclassification, and ensuring token standards include manual override and rapid remediation mechanisms to prevent consumers being unfairly blocked or locked out of their assets.
- Ensuring privacy-by-design principles are built into token standards to prevent unnecessary exposure of transactional histories or personally identifiable information on public chains. The FCA should encourage the adoption of standards such as the Ethereum-based token standard ERC-3643, which incorporates eligibility (KYC), jurisdictional flags, permissioned controls and interoperability features. Standards should also promote secure encryption, off-chain data management, and compliance with data protection laws.
- Allowing firms to test tokenised registers within controlled environments and/or through Provisional License, requiring them

to report incidents and consumer outcomes to inform regulatory best practice.
- Mandating public reporting of smart contract incidents, audits, and remediation steps to enhance transparency and build trust in tokenised systems.
- Managing concentration and operational risks by setting oversight requirements for platforms that consolidate multiple wallets, ensuring resilience and continuity planning.
- Supporting the development of interoperable token standards that enable consumers to switch between platforms or providers without losing functionality or access to their assets.
- Requiring firms to demonstrate, before live operation, how consumer protections will function under various failure scenarios (e.g., bugs, outages, or misclassifications).
- Ensuring firms are future proof against emerging risks such as quantum computing, to protect consumers' encrypted data over the long-term including transitioning to quantum-resistant cryptography to safeguard sensitive data against future decryption threats.
- Enhancing consumer capability and understanding by requiring firms to explain tokenisation risks and operational processes in plain, accessible language.

Managing network risks

5 Do our COLL rules and proposed guidance provide sufficient flexibility to support fund tokenisation use-cases that use public networks?

The FCA's COLL rules and proposed guidance provide a flexible and forward-looking foundation to support fund tokenisation using public networks. However, from a consumer protection perspective, there remain significant gaps in legal clarity, operational resilience, and investor communication that could lead to inconsistent outcomes for retail investors. These areas require further clarification and minimum standards to ensure that innovation does not compromise retail investor safeguards.

Under COLL 9, which governs overseas schemes, the use of public blockchains introduces complex jurisdictional challenges. When nodes, validators, and smart contracts are globally distributed, the legal clarity around ownership, enforcement, and investor protection becomes uncertain. Current rules do not clearly specify how UK law governs consumer rights when fund registers are maintained across

international networks. The Panel therefore recommends that the FCA establish a clear legal-domicile test and registry requirements to define how distributed ledger records can satisfy the UK domicile and accessibility obligations under COLL and the OEIC Regulations.

Under COLL 6, which sets out operational requirements, there is currently insufficient prescriptive detail on contingency planning and resilience for DLT-based models. The absence of minimum standards for network outage procedures, recovery timelines, and cost allocation during failures may result in uneven protection for investors. The Panel recommends that the FCA set a minimum contingency and testing regime, specify recovery protocols for smart-contract and network outages, clarify responsibility for operational costs, and mandate smart contract standards, including off-chain record backups, audit trails, and independent code audits.

Finally, under COLL 4, which covers information to unitholders and depositaries, tokenised fund structures require clearer guidance on communication and accessibility. Investors and depositaries should be able to inspect records without needing blockchain fluency or private keys, and on-chain risks such as outages, and custody loss should be clearly disclosed. The FCA should therefore require plain-language, DLT risk disclosures and standardised, user-friendly inspection mechanisms.

While the COLL framework is adaptable, further clarification on legal domicile, resilience standards, and investor communication is needed to ensure that tokenisation on public networks enhances efficiency without diluting consumer protection.

Chapter 3: Fund efficiency and direct dealing in authorised funds

6 Do the proposals in this Chapter provide adequate flexibility for firms considering tokenisation and the migration to T+1 securities settlement?

We recognise that the proposals in Chapter 3 introduce a valuable degree of operational flexibility for firms as they prepare for both the transition to T+1 securities settlement and the potential adoption of tokenised fund structures. Allowing authorised funds or their depositaries to act as principal in unit transactions, rather than the Authorised Fund Manager (AFM), represents a forward-looking reform that can simplify processes and reduce inefficiencies in back-to-back dealing.

However, while the proposals may be operationally flexible for firms, they also introduce a number of potential risks and uncertainties from a consumer perspective, which warrant careful consideration and additional safeguards.

Under the proposed direct dealing model, the counterparty to an investor's transaction would change from the AFM to either the fund or its depositary. This shift may obscure lines of accountability in cases of pricing errors, transaction failures, or complaints. Retail investors may not readily understand who is responsible for resolving disputes or ensuring the fair execution of unit transactions. To protect consumers, the FCA should require firms to provide clear, standardised disclosures explaining who the investor's contractual counterparty is, and who bears responsibility for key functions such as pricing, settlement, and complaint resolution.

The industry may face the challenge of implementing multiple structural changes simultaneously. While each initiative has merit, concurrent implementation raises the likelihood of operational disruption. Systems mismatches, valuation errors, or delays in settlement could temporarily disadvantage investors, particularly those relying on the timely redemption of fund units. A pilot-based approach to adoption, possibly through a Provisional License approach, would help ensure that operational risks are identified and mitigated before widespread rollout, especially for retail-facing funds.

Tokenisation introduces new forms of technology and cybersecurity risk. Failures in smart contracts, data recording, or token transfer mechanisms could directly impact investors' ability to access or verify their holdings. The Panel recommends that the FCA considers mandating robust testing, audit trails, and contingency arrangements for tokenised structures before they are permitted to replace existing systems of record.

Retail investors may struggle to understand how direct dealing, tokenisation works. Without clear and accessible communication, there is a risk of diminished confidence and trust in the authorised fund sector.

While the proposals provide adequate flexibility for firms, they do not yet guarantee adequate protection and clarity for consumers. To achieve a fair and balanced transition, we recommend that the FCA:

- clarify roles and responsibilities among AFMs, funds, and depositaries under the direct dealing model.
- phase the introduction of direct dealing alongside T+1 and tokenisation initiatives.

- introduce specific consumer disclosure standards addressing counterparty, pricing, and settlement responsibilities.
- require comprehensive operational testing and risk assessments for tokenised funds.

Alternative operating model

7 Do you support the introduction of an optional regime to allow for direct dealing in authorised funds?

We support the principle of introducing an optional regime for direct dealing, including the Direct2Fund (D2F) model, as it offers the potential to modernise the operational framework of authorised funds, reduce inefficiencies, and align the UK with global fund domiciles. However, from a consumer protection and operational resilience perspective, we believe several important safeguards and clarifications are necessary before widespread adoption can occur.

As per our response to DP23/2, the Panel would like to reiterate the need for the FCA to include a comprehensive risk assessment on the implications for consumers using existing models, as well as for those who adopt new technology. While the proposed Direct2Fund (D2F) model may create operational efficiencies and align the UK with international practice, the consumer impact of running both the traditional principal model and the new direct dealing model in parallel must be fully understood.

For example, what happens if a given fund is offered both through the traditional and new Direct2Fund models? To what extent might older or more vulnerable consumers be disadvantaged if they are less able to engage with or understand the new dealing structure? There is a risk that investors could face unequal access to information, differing settlement timelines, or uncertainty over who bears responsibility in the event of transaction errors or delays.

The Panel also notes that the D2F model changes the accountability and operational framework by reducing or eliminating the AFM's intermediary role. While this could streamline processes, it also raises questions about who is responsible for safeguarding investor interests, ensuring fair pricing, and managing operational failures. Accordingly, the FCA should assess whether this shift would require direct supervision or regulation of portfolio managers, funds or depositaries offering Direct2Fund options, to maintain equivalent standards of consumer protection and prudential oversight.

The current principal model provides clear investor safeguards when cash is held by the AFM during settlement. While direct dealing may

reduce the AFM's exposure, it may also shift custody and settlement risks to other entities. The FCA should confirm how client money protections and compensation schemes will apply when investors transact directly with the fund or depositary. Consumers should not be exposed to greater risk of loss in the event of an operational failure or insolvency merely because the dealing structure has changed.

In summary, the Panel supports the principle of providing firms with greater flexibility through an optional direct dealing regime. However, this flexibility must be accompanied by:

- A clear assessment of consumer risks and distributional impacts, particularly for vulnerable investors;
- Clear disclosure obligations explaining who the investor's counterparty is and who is responsible for ensuring fair execution and settlement.
- Standardised communication protocols between AFMs, depositaries, and investors to avoid confusion about points of contact and liability in case of failed or delayed transactions.
- Defined accountability and redress mechanisms to protect investors under both models; and
- Maintain robust client money and insolvency protections equivalent to those under the current model.
- Ongoing regulatory oversight to ensure consistent standards of governance, transparency, and investor protection across all dealing structures.

Impact on Handbook. Issues and Cancellations Account

8 Do our proposed requirements for operation of the IAC provide a proportionate control environment while ensuring funds are operated, and overseen, in line with principles of segregated liability?

The Panel supports FCA's proposal to introduce Issues and Cancellations Account (IAC) to manage cash flow under the D2F model provided that:

- consumers receive clear disclosure explaining how investor money is processed and protected under direct dealing arrangements. In particular, consumers receive clear pre-transaction disclosure about payment obligations and consequences of transaction failures, late or non-settlement and pricing-mismatch.

- AFMs and depositaries are accountable for IAC operation, including oversight of umbrella-level accounts.
- segregation of sub-fund assets is strictly enforced.
- rules are set requiring AFMs to
    - attribute incoming payments promptly to the correct sub-fund and unlocated sums are ringfenced, returned or moved into a client money account by the next business day.
    - cover interest costs or bear costs where they did not cancel failed deals.
- rules are set requiring IACs to not go overdrawn or allow one sub-fund's cash to cover another's obligations.
- reconciliation and attribution rules are applied daily, with unallocated sums promptly returned or ring-fenced.
- omnibus IAC structures are subject to a risk assessment and sign-off confirming they do not expose investors to contagion or cross-fund risk.

9 Do you agree with our proposals in respect of overdrafts and limits on fund exposure to a given bank or group? If not, why?

The Panel in principle agrees with the proposed bank exposure and overdraft limits. While flexibility for operational efficiency may be good for firms, retail investors must not bear the risk of concentrated bank exposure and short-term borrowing that they neither control nor benefit from.

As per our earlier response, the Panel supports the FCA's intention to maintain prudential safeguards that limit a fund's exposure to a single bank or banking group. We remain concerned that the proposed flexibility around overdrafts and concentration limits could introduce hidden risks for retail investors.

Allowing funds to exceed the 20% deposit exposure limit or to utilise overdrafts, even if temporarily, increases counterparty and concentration risk. In the event of a bank failure or liquidity stress, investors could experience delays in redemptions or potential loss of value, undermining confidence in authorised funds. As those exposures are operationally complex and largely invisible to end investors, who would reasonably assume that their investments are fully diversified and not subject to short-term credit or liquidity risks.

In particular, the use of overdrafts can raise concerns that investor money may be indirectly used to fund settlement mismatches, potentially blurring the principle of segregated liability between sub-funds. Such scenarios could disadvantage consumers and create contagion risk within umbrella structures if not strictly controlled.

The Panel therefore recommends that:

- Diversified bank exposure is enforced to remove concentration of single bank exposure particularly when a bank fails.

- FCA

    - maintains the 20% exposure limit to any one bank or group as a core consumer safeguard, with any temporary breach strictly time-limited and reported to the depositary and the FCA.
    - clarifies that overdraft facilities should only be used in exceptional, short-term circumstances and must not form part of routine fund liquidity management.
    - requires AFMs to absorb any interest or overdraft costs that arise from operational delays, rather than passing them on to investors.
    - strengthens depositary oversight to include active monitoring and escalation where overdraft or exposure limits are approached.

While we recognise the need for operational flexibility under the D2F model, this should not come at the expense of consumer protection. The FCA's final rules should ensure that any exposure to a single institution or temporary borrowing arrangement is appropriately limited, transparent, and overseen to safeguard investors' capital and maintain market confidence.

10 Do you agree we should include all cash held at a given bank within our spread of risk rules for UCITS and NURS? If not, why?

The Panel agrees in principle that all cash held at a given bank should be included within the spread of risk rules for UCITS and NURS, as this maintains consistency in how counterparty exposures are measured,

reinforces prudent diversification and provided it continues to provide strong depositary oversight.

In particular, the Panel agrees with the FCA's proposals regarding the application of the spread of risk and bank exposure rules to funds operating under the Direct2Fund (D2F) model.

The Panel also supports the continued requirement that no more than 20% of a fund's property may be held as deposits with a single bank or banking group, including cash held within an Issues and Cancellations Account (IAC). The Panel agrees that this approach maintains important diversification safeguards and ensures that investors are not unduly exposed to the failure of a single financial institution.

The Panel also considers it appropriate that IAC balances and any overdrafts are included within the exposure calculation, even when such balances are held only temporarily for settlement purposes. This provides a consistent and transparent measure of risk across all forms of fund-held cash.

We also support the FCA's proposal to withdraw the existing guidance that excludes income cash held with the depositary's group from the exposure calculation. Given developments in fund cash management and diversification practices, it is reasonable that all cash holdings — including income or uninvested cash — should be subject to the same 20% exposure cap. The proposed 12-month transition period appears proportionate, allowing firms sufficient time to adapt operationally without unnecessary disruption.

The Panel further agrees with the FCA's approach to temporary breaches of these limits as long as those breaches are strictly time-limited and reported to the depositary and the FCA. The Panel believes that allowing forbearance where a breach arises from circumstances beyond the AFM's or depositary's control (such as large subscriptions or redemptions) is a pragmatic and proportionate measure. The Panel also agrees that any excess exposure must be resolved promptly in the interests of unitholders.

Overall, the Panel believes these proposals strike the right balance between prudent risk management, operational practicality, and investor protection.

The IAC as Scheme Property

11 Do you agree with our proposed accounting controls in respect of use of IAC? If not, why?

The Panel agrees with the proposed accounting controls but requests stronger, clearer operational safeguards and explicit investor protections. In particular, the panel agrees with:

- treating unattributed sums as scheme property for exposure calculations.
- excluding sums that cannot reasonably be allocated from unit pricing.

The Panel recommends the following:

- time limits for reconciliation before funds must be returned to sender or moved to client money account (e.g 24 hours, with exceptions documented). This reduces credit and liquidity risks to investors.
- independent audit requirements for reconciliation and allocation decisions.
- mandatory disclosure in prospectus and investor materials about the status of IAC balances, the consequences in insolvency and FSCS applicability.

Finally, if AFM's use alternative accounting practices, FCA should consider requiring documented controls and information disclosure in the prospectus that the undertaking exists.

Consumers rely on accurate NAVs and clear protections for their cash. Without time limits, independent oversight and disclosure, the proposed approach leaves room for unfair pricing, opacity and undue credit risk.

12 Do you agree with our proposal to provide additional clarity on cash held by LTAF and the requirement to appoint an external valuer? If not, why?

Since the Long Term Asset Fund (LTAF)'S schemes is open for institutional investors, DC pension schemes and advised high-net-worth investors, the Panel agrees that since the scheme property is primarily externally-valued CIS/AIFs, the AFM should have discretion not to appoint an external valuer — provided that liquidity holdings (cash, gilts held for short-term liquidity) can be valued conventionally by the AFM. The Panel recommends that the AFM must publish in the

prospectus the classes of assets it will value internally and the valuation methodologies, and maintain documented governance demonstrating the AFM can reliably value these liquidity assets.

Investor Disclosures and Changes to Existing Schemes

13 Do you agree with our proposals in respect of investor disclosures and communications? If not, why?

The Panel agrees with requiring specific prospectus disclosure and resolving unattributed sums before schemes of arrangement — but ask for precise minimum disclosure wording and investor notice periods.

In particular, the Panel agrees with the FCA's proposal to require the prospectus of a direct-dealing fund to include a brief summary of the implications of using an Issues and Cancellation Account (IAC), particularly in cases of insolvency or payment failure. We support the intent to improve transparency and investor understanding of operational and credit risks associated with IACs.

The Panel recommends enhancing this disclosure requirement to ensure it is clear, concise, and comparable across all funds. The Panel recommends that the FCA mandates a short, standardised disclosure, such as a one-box summary, so that investors can easily compare funds' IAC arrangements and associated protections in plain language, covering:

- whether the IAC is treated as client money or scheme property;
- whether FSCS protection applies to cash held in the IAC;
- who bears the credit risk of the IAC bank while funds are held pending allocation or payment; and
- actions the Authorised Fund Manager (AFM) will take in the event of insolvency of either the fund or the IAC bank, including how unattributed sums will be reconciled, returned, or protected.

The Panel believes that this approach would promote clarity, comparability, and consumer confidence, while avoiding lengthy or inconsistent prospectus text that could obscure the key risks.

Overall, the Panel believes that innovation must not compromise investor protection. Disclosures must be engaging, personalised, and accessible via digital channels. Interactive tools such as apps, dashboards and digital interfaces should be used to help investors understand fund performance, compare products and make informed decisions. Finally, the Panel considers that consumer testing should be used to inform the development of regulation, particularly in relation to consumer disclosures.

The Panel further agrees that the introduction of direct dealing or use of an Investor Account (IAC) constitutes a notifiable operational change requiring prior notice to investors. To ensure clarity and orderly transition, the Panel recommends that the FCA define what constitutes "reasonable notice" within the rules or guidance. In our view, a minimum of 10 business days' notice should be required where bank account details for payments are amended, with a longer period where the change materially affects the fund's dealing mechanisms, timing, or settlement procedures. This will provide investors with sufficient opportunity to update payment instructions, confirm receipt arrangements, and understand any revised dealing process before the change takes effect.

The Panel also supports the proposal that, prior to any scheme of arrangement or fund split, all unattributed sums in an IAC must be identified and either transferred to a client money account or otherwise resolved. This is essential to prevent remaining investors from bearing an unfair concentration of credit risk to the IAC bank once the scheme assets are restructured. Where it is operationally impracticable to fully resolve unattributed sums beforehand, the Panel recommends that completion of the arrangement be conditional on trustee or depositary approval. These safeguards will help ensure that fund reorganisations do not inadvertently disadvantage continuing investors.

Responsibility for Anti-Money Laundering Controls and dealing with small sums arising from fund operations.

14 Do you agree that fund AFMs should bear the cost of exercising discretion for late payments? If not, why?

The Panel agrees that AFMs should bear this cost. Late payments or administrative delays are generally within the AFM's operational control, not the investor's. It also reinforces accountability, ensuring AFMs invest in efficient payment systems. Passing such costs to consumers would be unfair. To the same extent, the Panel believes that AFMs should be allowed to recover full or partial costs if delays are caused by the investor (e.g., providing incomplete details).

15 Are there scenarios where this may not be appropriate or such costs should be allocated differently?

The Panel believes that as a default such cost shall be the AFM responsibility unless investor behaviour, as described above, directly contributes to the cost. For example, if the investor's own actions cause the delay, then such costs could reasonably be shared or charged to the investors. The Panel recommends that FCA should provide clarity as to when such discussions can occur.

16 Do you support introducing broader powers to deal with historic orphan monies? What legal or regulatory barriers might prevent introducing such a process?

The Panel supports the introduction of broader powers to deal with historic orphan monies, as this would enable the efficient closure of dormant or legacy funds and allow for the possible allocation of unclaimed sums to societal projects. However, the Panel identifies the following potential barriers to implementation: limited access to investor information due to data protection and privacy laws, and the fact that consumers remain the legal owners of these monies and may object if they feel decisions about their funds have been made without their consent.

Chapter 4 – Fund tokenisation roadmap

Tokenised Money Market funds and supporting the use of stablecoins to settle unit deals.

17 Are there any other purposes for which funds, fund managers, or investors may need to hold cryptoassets to support fund operations on-chain?

Beyond settlement and gas fees fund managers may need to hold cryptoasset as a

- collateral during temporary short-term liquidity needs when the fund moves assets on-chain and until transaction is confirmed During this gap, the fund might need to hold a temporary amount of tokenised collateral to keep the liquidity flowing.
- liquidity buffer for intraday settlement so that transactions can settle instantly
- utility token to be able to operate on the blockchain network.

Any such holdings must be limited for the use, custodially segregated and excluded from core investments.

18 Would our potential amendments to COLL provide sufficient flexibility for firms to use digital cash and money like instruments for operational purposes, including unit dealing?

As described in our answer for question 5, the Panel believes that amendments to COLL can provide further consumer protection in terms of legal clarity, operational resilience, and investor communication. Further to the clarification and minimum standards discussed in our

previous answer, the Panel would like to recommend that FCA allows digital cash and qualifying stablecoins only for operational purposes and not as a discretionary investment unless explicitly authorised by the FCA. Also, that only recognised stablecoins that meet the qualifying stablecoin definition to be allowed for operational purposes. The Panel also recommends that the FCA imposes a cap on exposures and mandatory segregation of operational tokens, limits who can hold them (AFM, fund and depositary) and auditability requirements. Finally, that the FCA require investor disclosure and suitability checks in line with Consumer Duty requirements.

19 Would a limited sandbox or standard waivers/modifications be appropriate routes to allow us to develop a final regime in collaboration with industry? What features may be desirable in such a regime?

The Panel agrees that sandboxes, Provisional License and, where appropriate, targeted waivers can be provided in collaboration with the industry and consumers and should embed consumer protection as a core condition. Accordingly, the Panel recommends the following:

- Pilots should explicitly define the investor type (retail or institutional) to enable a focused understanding of the specific challenges and opportunities within each segment.
- Retail participation should initially be restricted unless additional safeguards—such as clear warnings and disclosures—are implemented.
- Firms should utilise the Bank of England and FCA's Digital Securities Sandbox (DSS).
- Firms should adopt standardised risk warning templates and ensure clear complaint and redress mechanisms are in place for pilots and consumer-facing documentation, to support consumer comparability.
- Firms must have audited smart contracts, conduct reconciliation testing, and establish contingency procedures for potential outages.
- Pilots should clearly explain consumer rights to exit or transition from a plan if the token or chain becomes unsupported during the pilot phase.
- Lastly, firms must ensure that consumer data privacy and anti-money laundering (AML) controls are applied throughout the pilot phase.

20 Do any other areas of our rules conflict with or prevent use of digital cash instruments or money-like instruments for unit dealing, distribution payments, or for payment of charges and fees?

COLL 6.2.13R expects the Authorised Fund Manager (AFM) will arrange for payment of cash or cleared funds to the Investment Company with Variable Capital (ICVC) or depositary following the issue of units. Where a fund uses direct dealing, investors are contractually obliged to make this payment. Without an amendment to the rules, this requirement may prevent investors to make these payments using alternative settlement assets.

The definition of what constitutes a *deposit* or *money* could affect whether tokenised deposits qualify as "cash" for regulatory purposes. COLL 6.2.13R refers specifically to cash or cleared funds. Without a rule amendment, this could prevent the use of tokenised cash as the primary settlement medium. The chapter recognises that technical changes are required, as the current language reflects traditional settlement mechanisms and does not explicitly include tokenised or digital settlement assets. Unless interpreted broadly or amended, the use of tokenised cash as the primary settlement medium may not currently comply with this rule.

As per consultation paper (CP25/14[8]) existing custody rules assume traditional custodians and settlement systems; crypto custody models (private keys, smart-contract custodians) may not map cleanly onto these frameworks without additional guidance or rule modifications.

Rules concerning segregation and client asset protections may also need to be adapted for tokenised assets to ensure that investor claims are preserved in the event of insolvency.

21 Would our existing rules, including the Consumer Duty, provide enough protection for investors if we allow a fund to hold cryptoassets for settlement and fund operational purposes only?

Tokenised Financial Assets

As per our previous consultation responses including our CP25-14 response on the Discussion Paper on the proposals for regulating stablecoins and cryptoassets custody, the Panel continues to recommend retaining the Consumer Duty (CD) for all cryptoasset activities (including

[8] CP25/14: Stablecoin issuance and cryptoasset custody | FCA

those that allow a fund to hold cryptoassets), supported by specific rules and guidance to address sector-specific risks. CD alone is insufficient due to the complexity and rapid evolution of cryptoasset market.

Consumer Duty alone is not sufficient. The Consumer Duty focuses on firms delivering "good outcomes" (like fair value and clear information) and not how firms can guarantee those outcomes—especially in complex areas such as cryptoassets. Although the Consumer Duty provides important baseline protections for consumers, it does not address the specific risks of cryptoassets. Without specific rules on transparency and disclosure, there’s a high risk of uninformed decision-making—even when firms act “fairly” under the Consumer Duty.

We are therefore currently of the view that the FCA should adopt a blended approach to regulating cryptoasset activities, which involves:

- Maintaining the CD in place for all cryptoasset activities, subject to the following:
- Introducing targeted cryptoasset specific rules to address known risks, areas of specific consumer harm, and areas where the application of the CD poses particular challenges; and
- Introducing specific targeted guidance to supplement the above, particularly in relation to addressing some of the areas where the application of the CD requires further clarification.

Our suggestion is not about drowning the sector in regulation. Rather it is with the intention of introducing clarity as well as an adequate level of consumer protection.