THE LAW COMMISSION'S CONSULTATION ON THE DRAFT BILL ON OBJECTS OF PERSONAL PROPERTY RIGHTS

CLLS FINANCIAL LAW COMMITTEE RESPONSE

INTRODUCTION

The City of London Law Society (CLLS) represents approximately 15,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multijurisdictional legal issues.

This Response to the Law Commission's Consultation on its short draft Bill (the "**Bill**") on objects of personal property rights (the "**Consultation**") has been prepared by the Financial Law Committee ("**FLC**") of the CLLS, whose members specialise in major financings involving obligors incorporated in multiple jurisdictions, creditors incorporated or doing business in multiple jurisdictions, and assets located, or deemed by principles of private international law to be located, in multiple jurisdictions. Concepts of English law and other laws relating to digital assets, and the development of these concepts, are increasingly critical to the transactions and advisory matters on which members of the FLC advise. Full details of the members of the FLC appear on the CLLS website. Members of the FLC who are partners of Clifford Chance LLP,.Linklaters LLP and Norton Rose Fulbright LLP have taken no part in the preparation of this Response and have notified the Chairman of the FLC that their firms are submitting their own response to the Consultation in which they take a different view on a number of issues from that expressed in this Response; those members have, accordingly, notified the Chairman that they and their firms do not wish to be associated with this Response by reason of their membership of the FLC.

The FLC continues to appreciate greatly the thorough work and detailed analysis undertaken by the Law Commission with regard to the legal issues that arise in the context of digital assets, including the Call for Evidence on conflict of laws aspects issued in February 2024. As the FLC noted in its response dated 4 November 2022 (the "**Response**") to the Law Commission's Consultation Paper on Digital Assets issued in July 2022 (the "**July 2022 Consultation Paper**"), and as has also been recognised by the UK Jurisdictional Taskforce (the "**UKJT**"), the very nature of most types of digital assets has given rise to, and will continue to give rise to, complex cross-border legal issues, and we fully support the Law Commission's ongoing work in this area.

We set out below the FLC's responses to the three questions listed in paragraph 4.10 of the Consultation. First, we set out some introductory comments on the draft Bill.

We agree that the development of English law in this area is, as a general matter and subject to specific targeted legislative reforms, best left to the common law and principles of equity, which have proven to be more than up to the task of evolving over time in England and Wales and in other common law jurisdictions. The case law developed by the English courts over the past decade itself demonstrates the willingness of judges to use existing and well-established principles of law to address issues arising

from the creation and development of digital assets. We note, and agree with, the commentary in the Consultation that most of the cases over the past decade in which the English courts have considered the nature of crypto-tokens and other digital assets have been interim or interlocutory applications which may not have required, or permitted, detailed analysis of the legal nature, or the proper and most coherent categorisation, of the assets in question. We also note, as was explained in the July 2022 Consultation Paper (and in the Law Commission's Final Report issued in June 2023 (the "**Final Report**")), that the proper scope of the concept of a "thing in action" as a matter of current common law remains undetermined and, indeed, is subject to considerable academic debate. Nonetheless, there is a clear trend of development of the common law and principles of equity in this area, with more substantive judgments issued by senior English courts recognising the ability of crypto-tokens and other digital assets to be the objects of personal property rights. The fundamental question is, it seems to us, whether the Bill is needed at all. In the view of the FLC, it is not, or, not at this point in time. If, notwithstanding our view, a short legislative instrument is considered desirable to provide clarity or support legal certainty in this area, for the reasons we set out in our response to Question 1 below, we do not consider that the Bill in the form proposed in the Consultation achieves those objectives. We have proposed changes to the draft Bill (set out in the Annex and explained in our response to Question 1 below) to support the achievement of those aims and to minimise the risk that the Bill, were it to be enacted, might inhibit a proper policy-based evolution by the English senior courts of the common law principles and related taxonomy for personal property rights as affecting digital assets.

It may be that the ongoing work of the Law Commission in this area, including the most recent Call for Evidence on conflict of laws issues, will identify lacunae in English law which would benefit from assistance in the form of statutory provisions. We are also interested to see the Statement which the UKJT has recently indicated it will issue in April 2024 following its recent consultation on digital assets and English insolvency law. At the moment, however, we are not convinced that the introduction of the Bill (in the form proposed in the Consultation) is necessary or helpful.

In our Response, we indicated our concerns regarding the "third category" of personal property suggested in the July 2022 Consultation Paper Although we note that the Final Report addressed some of these concerns, and the Consultation itself reflects the preference to leave the development of English law in this area largely to the judiciary, we are concerned that the Bill may result in fettering the ability of judges of the senior English courts to develop the law in a coherent manner, reflecting and expanding upon the existing jurisprudence. We note, also, that the law applicable to digital assets cannot be viewed without also considering the regulatory environment in which numerous persons operate, including investors in and users of digital assets and those providing finance for the acquisition of, or secured by, digital assets. We appreciate that not all persons who deal with digital assets operate in a regulated environment, but many do, and it is critical that the regulatory environment reflects, so far as possible (noting again that principles of private international law are almost invariably engaged when dealing with digital assets), accepted legal characteristics of these types of personal property and the rights, obligations and restrictions to which these characteristics give rise. To take an obvious example, there are well-developed principles applicable to the custody of financial assets in English law and UK financial services regulation, founded principally on trust law concepts developed with respect to intangible assets; we are concerned that any development of a "third type" of personal property for digital assets subject to custody arrangements, potentially attracting legal concepts loosely analogous to those developed for things in possession (e.g. bailment), would cloud and confuse the law in this area and the associated regulatory regimes.

RESPONSES

Our responses to the three questions raised in the Consultation are set out below.

1. **Do you agree with the general approach of the draft Bill, and agree that it will achieve the desired effect?**

1.1 We are concerned that the Bill is drawn too widely for a legislative instrument potentially affecting the personal property rights of businesses or individuals. We understand that the mischief to which the Bill is addressed is the perceived need to provide clarity and certainty as to the capability of an intangible thing (that is not a thing in possession, i.e., a thing/chose that is capable of possession whether under the common law or by statute) to be the object of personal property rights. For the reasons explained further below, in order to address any concerns regarding the effectiveness and enforceability against the world of rights in relation to an intangible asset that is not a thing in possession and exists independently of the legal system or of persons (including crypto-tokens and other similar digital assets), we suggest that clause 1 of the Bill should be amended so that it reads:

> "*A thing is capable of being the object of personal property rights even though it is neither -*
> *(a) capable of possession, nor*
> *(b) a right that may only be claimed or enforced by legal action or proceedings against another person or persons*."

This wording would limit the scope of the clause to deal specifically with its targeted mischief i.e. to clarify that a thing may be the object of personal property rights, even though (to use the language of the Consultation) it is not a thing in action "in the narrow sense". For the reasons we explore further below, we believe it would be unhelpful for the Bill to adopt the undefined term, "thing in action", as a central concept to determine the scope and effect of the legislation. We consider it essential that what is intended by the term "in the narrow sense", as outlined in the July 2022 Consultation Paper, the Final Report and the Consultation, be unpacked and set out specifically in the Bill in order to support its objectives of clarity and legal certainty.

Consistent with our suggestions above, we also suggest that the title of the resultant Act be amended so that it does not refer expressly to digital assets.

A revised draft of the Bill, reflecting our suggestions above, is set out in the Annex.

1.2 The Consultation itself recognises that the proper scope of the concept of a "thing in action" is, as a matter of our current common law, uncertain, although as we noted in our introductory remarks and as recognised in the Consultation, it is clear that English law is moving in the general direction of recognising that crypto-tokens and other similar digital assets may be the object of personal property rights. The analysis at paragraphs 4.29 to 4.38 of the July 2022 Consultation Paper and at paragraphs 3.35 to 3.42 of the Final Report underlines that, at present, there remains a material degree of judicial and academic debate as to what may or may not properly be regarded as a "thing in action" as a matter of common law. Specifically, it is possible that, notwithstanding the first instance decisions made as part of interim or interlocutory proceedings, the common law might (absent the Bill) develop to recognise a "residual" concept of a thing in action, i.e., as embracing all categories of intangible personal

property that are not choses in possession (the "wide view"), and not the "narrow view" adopted by the Consultation supporting the Bill (i.e., that which conceptualises a thing in action as being limited to a right that can only be claimed or enforced by legal action or proceedings). This uncertainty under the existing common law is emphasised by the repeated use of the phrase "in the narrow sense" throughout the Consultation when referring to the concept of a thing in action as contemplated by the Bill. To our mind, this approach recognises that, absent the Bill, there remain potentially two senses in which the English courts (and, in particular, the English senior courts) might ultimately determine how the concept of a "thing in action" should (as a matter of English personal property law) be interpreted and applied. There is already, for example, evidence in existing case law and in academic commentary that the dictum of Fry LJ in *Colonial Bank v. Whinney*[1] is neither exhaustive nor dispositive, or may indeed have contemplated an expansive and dynamic interpretative approach to what may fall within the scope of a "thing in action"[2].

1.3 This use of the undefined term "thing in action" in clause 1 of the Bill runs the risk of creating legal uncertainty. As the Bill itself does not appear to be (and, for the reasons outlined above, cannot be) a declaratory enactment, the use of the term in clause 1 potentially creates other wider issues. Even though the scope of the term is in itself uncertain as a matter of the existing common law, the implicit effect of clause 1 is to require the term to be given some form of narrow interpretative scope. If the Bill supported a wide view of the concept of a "thing in action", there would be no need for the additional category of personal property that is supported by clause 1 as all things that are not amenable to or capable of possession, but which are intended to remain capable of being the object of personal property rights, would be or would fall within the category of "things in action".

1.4 As a consequence, the Bill is not simply clarifying the common law and does not act as a declaratory enactment. Absent the Bill, it would remain open to the Court of Appeal or the Supreme Court to recognise crypto-tokens and other digital assets as falling within the scope of an expanded concept of a chose or thing in action. The Bill, as drafted, pre-empts any such common law development and effectively provides a statutory declaration that the concept as a matter of common law is to be limited to a right that can only be claimed or enforced by legal action or proceedings (i.e. the "narrow view" of the term, "thing in action"). The policy objective of the Bill does not require such a declaration to be made by Parliament – the English courts may themselves determine that a crypto-token or other digital asset is the object of personal property rights by including them within a taxonomy for personal property that includes the "wide view" of what a thing in action is.

1.5 A further concern with the declaration implicitly being made by the Bill is that a non-declaratory enactment potentially creates issues for the presumption of non-retrospectivity where a retrospective application of an enactment can cause unfairness for those affected by it (see Bennion, Bailey & Norbury on Statutory Interpretation, Eighth Edition (2020) at paras. 7.13 and 7.14). For example, if a person (prior to the

[1] (1885) 30 Ch.D. 261 at 285

[2] In this context, we note that in a recent decision of the Singaporean High Court, issued after publication of the Law Commission's Final Report, the judge concluded that the crypto assets the subject of the litigation were things in action and that the category of things in action as a matter of common law is "broad, flexible and not closed": see ByBit Fintech Limited -v- Ho Kai Xin & Ors. [2023] SGHC 199 at paragraphs [34] and [35].

Bill's enactment or proposed enactment), and reasonably relying on an interpretative analysis of the existing common law that all intangible things that are not choses in possession are choses in action, were to take a charge over the chargor's "choses in action" believing (with the chargor) that this term (as a matter of law) includes the chargor's crypto-tokens and other digital assets, the Bill, as drafted, if given retrospective effect, would now remove crypto-tokens and other digital assets from the scope of the relevant charging clause. This would prevent the chargee (contrary to its legitimate expectation or belief and the chargor's intention) having an equitable proprietary interest in the relevant digital assets of the chargor. This potentially raises the concern that the Bill could retrospectively, unnecessarily and unfairly prevent the chargee's peaceful enjoyment of its property for the purpose of the European Convention on Human Rights, or otherwise operate unfairly upon the legitimate interests or expectations of parties affected by the Bill. In order to avoid such a result, a court might therefore use the presumption against retrospectivity and apply the Bill only to things that arise or are created, or proprietary rights or interests that arise or are created in or in relation to intangible things (not amenable to possession), after the Bill comes into force. That approach would, though, defeat one of the key purposes of the Bill, which is to clarify the law of personal property rights as applicable to crypto-tokens and other digital assets (as well as proprietary rights or interests in or in relation to such assets) howsoever and whensoever arising or existing – and so avoid "two tiers" of personal property rights in or in relation to digital assets dependent upon the time they are considered to exist or arise. This could also raise material legal uncertainty as to the practical application of the Bill, once enacted, as affected by difficult temporal issues relating to when a digital asset, or relevant right or interest, is to be considered to exist or arise so as to be properly within or outside the scope of the Bill's operative provisions.

2. **What do you consider the positive impact of the Bill to be? Could you quantify them [sic] (for example, by how much in £ or days/hours might a dispute be reduced)?**

2.1 We do not consider that there will be a positive impact of the Bill, for the reasons stated in our introductory comments and in our response to Question 1. As the Consultation rightly notes, in our view, the substantive law should continue to be developed by the common law and principles of equity, and we do not believe that much, if any, time or costs will be saved by the introduction of the Bill. We are also concerned that the Bill, at least in the form proposed by the Consultation, will limit the ability of the English senior judiciary to develop the law in this area robustly, coherently and consistently with other common law jurisdictions.

3. What do you consider the costs and/or risks of the Bill to be?

3.1 It is not possible to determine with any precision the costs that may be incurred if the Bill is enacted. Possible categories of potential costs would include (a) litigation arising from the concern we raise in paragraph 1.5 above regarding the temporal scope or limitations of the Bill (notably, whether it would, or would not, have retroactive effect), and (b) the costs that may be incurred by regulatory authorities in determining, and perhaps seeking advice in connection with, the extent to which the Bill (or the potential developments in English personal property law that the Bill may be taken to support adopting possessory-like concepts) may impact upon regulated activities, including (i) the safeguarding and custody of digital assets and the distribution of digital assets in the event of an insolvency of the custodian or any other person who

has a personal property right to those digital assets, and (ii) whether it is correct, for the purposes of determining regulatory capital requirements, to assume that regulated custodians should hold capital against operational risk but not necessarily against counterparty risk or market risk. The Law Commission may wish to raise this question directly with the Prudential Regulation Authority and the Financial Conduct Authority. These areas of potential uncertainty and litigation may affect precisely the most sensitive areas for the financial markets in the UK - the allocation of resources to persons with proprietary interests and creditors without such interests in cases where a failed business may hold an insufficiency of assets to satisfy all claims - an area where the scope for expensive litigation should be minimised as the associated costs will likely reduce the asset pool further and may place additional costs on parties already suffering, or potentially exposed to, substantial losses. Issues such as these will need to be considered and developed in any event, but it is not clear that the Bill (or wider principles of English personal property law that it may be taken to support) will provide any meaningful assistance in resolving them.

3.2 As regards the risks associated with the enactment of the Bill in its current form, or at all, we refer to our introductory comments and our response to Question 1.

ANNEX
Suggested Revised Draft Bill

A

BILL

TO

Make provision about the types of things that are capable of being objects of personal property rights.

BE IT ENACTED by the King's most Excellent Majesty, by and with the advice and consent of the Lords Spiritual and Temporal, and Commons, in this present Parliament assembled, and by the authority of the same, as follows: -

1. **Objects of personal property rights**

A thing is capable of being the object of personal property rights even though it is neither –

(a) capable of possession, nor

(b) a right that may only be claimed or enforced by legal action or proceedings against another person or persons.

2. Extent, commencement and short title

(1) This Act extends to England and Wales only.

(2) This Act comes into force at the end of the period of two months beginning with the day on which this Act is passed.

(3) This Act may be cited as the Property (Objects of Personal Property Rights) Act 2024.