

Digital Assets in Scots Private Law

Note for Consultation: May 2022

Response – June 2022

This response is provided by Dr Alisdair MacPherson and Dr Burcu Yüksel Ripley of the Centre for Commercial Law at the University of Aberdeen.

We welcome this consultation and appreciate the opportunity to provide our comments. We have a particular interest in this area of law and have been involved in previous consultations regarding related matters. Along with other members of the Centre for Commercial Law, we responded to the UK Government's Consultation and Call for Evidence on the UK's Regulatory Approach to Cryptoassets and Stablecoins (March 2021), the Law Commission of England and Wales (LCEW)'s Call for Evidence on Digital Assets (July 2021) and the LCEW's Consultation on Digital Assets: Electronic Trade Documents (July 2021). Our responses are available at the following link: <https://www.abdn.ac.uk/law/research/centre-for-commercial-law/public-policy-stakeholder-engagement-1109.php#panel1114>. We are also two of the co-authors of the United Kingdom (UK) Report for the International Academy of Comparative Law's General Report on Cryptocurrencies (Asunción 2022 General Congress, Topic IX.C), which gives attention to the law of England and Wales, the law of Scotland and private international law/conflict of laws issues, where appropriate.

Questions

- i. **The Expert Reference is strongly of the view that Scotland should participate in the reform of the law relating to electronic trade documents which has been proposed by the EWLC. Do consultees agree?**

We agree. There are compelling reasons to support the view that Scotland should participate in the law reform concerning electronic trade documents proposed by the LCEW and we will elaborate on some of them below.

First, Scotland defines itself as a trading nation with a strong and productive economy characterised by diverse businesses which are becoming increasingly more international. This is reflected in "Scotland: A Trading Nation", a plan for growing Scotland's exports. Since publishing the plan in 2019, the Scottish Government has been seeking to implement it. The plan is strongly aligned with Scotland's National Performance Framework localising and implementing UN Sustainable Development Goals. Participating in the reform of electronic trade documents would be a very positive step in this context and contribute favourably to Scotland's outlook in international trade.

Second, as we stated in our response to the LCEW's Consultation on Digital Assets: Electronic Trade Documents, there is a pressing need for law reform in the UK in this area to facilitate the use of technology in trade, provide legal certainty and predictability regarding the legal status of electronic trade documents, and give these documents the legal recognition that their paper counterparts have. We think that this will significantly help speed up the overdue transition to

paperless trade, which will better safeguard and maintain the global flow of information relating to the trade in goods and build resilience to shocks such as COVID-19.

Third, some of the Acts which will be affected by proposed law reform, such as the Bills of Exchange Act 1882 and the Carriage of Goods by Sea Act 1992, are also applicable in Scotland. If Scotland does not participate in the proposed law reform, that would result in divergence of the application of provisions within the legislation – despite the fact that the Acts are generally applicable in both England and Wales and Scotland. We do not think that this is desirable as it would potentially cause confusion and complications, divergence in trade practices in the UK, and, depending on the circumstances, intra-UK conflict of laws issues. In a broader international context, it might result in parties in international trade choosing the law of England and Wales to govern their transactions over Scots law and this may happen even in cases where Scots law would otherwise apply to the transactions in question.

ii. Do consultees consider that there are any remaining obstacles to applying the Electronic Trade Documents Bill in Scotland?

We don't consider there to be any significant obstacles to applying the Electronic Trade Documents Bill in Scotland. There would be however a need for training in the trade sector as well as the legal sector on the application and implications of the Bill.

iii. What do consultees consider would be the most effective way of participating in the electronic trade documents reform?

We consider that the most effective way to participate in the electronic trade documents reform is for representations to be made directly to the UK Government prior to publication of the draft Bill and for comments and other evidence to also be provided once the Bill has been brought before Parliament. The Scottish Government should express its support for the Bill's applicability to Scotland and the Expert Reference Group can play a key role in encouraging this and in providing expert input to the UK Government and other relevant parties. The Bill brought before the UK Parliament should extend to Scotland and the Scottish Parliament should provide the necessary resolution for devolution matters.

While the issue of electronic trade documents could be referred to the Scottish Law Commission (SLC) for consideration, we do not think this is desirable in the circumstances given that the Bill has been already listed in the legislative programme for the new UK parliamentary term. Involving the SLC would be time-consuming at this stage, lead to delays in applying positive law reform in this area where there is a pressing need for such reform, and would involve duplication of work already undertaken by the Expert Reference Group. As noted in this consultation paper, the LCEW received and acted upon responses from consultees in Scotland (including our own response to that consultation). Those responses appear to have been supportive of the notion that the proposed reforms could also usefully be applied to Scotland, and that was, and is, our view too. Given the apparent absence of controversy regarding the advantageousness of these reforms in relation to Scotland, the fact that the LCEW's consultation process involved consultees in Scotland and the Expert Reference Group has already considered the matter in detail and supports the application of the reforms to Scotland, we do not believe there is a need for separate or further consideration of the matter by the SLC or any other equivalent body.

iv. The Expert Reference Group considers that legislation is the most effective way of resolving uncertainty about the status and characteristics of digital assets in Scots private law. Do consultees agree?

Yes, we agree. We are of the view that Scots law could accommodate digital assets without bespoke legislation, particularly due to the flexibility and expansiveness of the meaning of property and property law in Scotland. Our expectation is that digital assets would be, in principle, considered property and identified as a special type of incorporeal moveable property. However, it may be a considerable period of time before there is sufficient case law to provide clarity regarding various aspects of digital assets from Scottish courts, especially since Scotland is a small jurisdiction and also some disputes are settled or resolved out of court. In the meantime, there would be uncertainty and this could impact upon the use of digital assets and affect decision-making of commercial parties. Legislating in this area may also send a positive message that Scots law supports and facilitates innovation in the digital space. As such, we see significant merit in using legislation to clarify the status and characteristics of digital assets in Scots private law. It will also allow for an approach that takes account of the views of different stakeholders, and offers more control over the particular rules to be adopted and their breadth, in comparison to case law which depends upon the cases that happen to arise and come before the courts.

v. What might be the scope of such legislation?

If there is to be legislation dealing with digital assets, it will be necessary to define “digital assets”. Of course, this will be a difficult task. The definition will need to be precise enough to capture the particular assets that are intended to be covered while being expansive and flexible enough to take account of technological developments and innovation that give rise to equivalent assets in the future. As well as material in the draft Electronic Trade Documents Bill (as noted above), other sources may assist in constructing a definition. A definition of cryptoassets is provided by the Money Laundering and Terrorist Financing (Amendment) Regulations 2019 (SI 2019/1511), which inserted Reg 14A into the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (SI 2017/692). It is stated that “‘cryptoasset’ means a cryptographically secured digital representation of value or contractual rights that uses a form of distributed ledger technology and can be transferred, stored or traded electronically”. As noted by this consultation paper, the plan would be to legislate in Scotland for digital assets beyond cryptoassets and so this definition would need to be amended to reflect technological neutrality, particularly to remove the reference to “cryptographically secured”. A definition of digital assets could expressly specify that certain assets such as cryptoassets fall within the definition, if that was considered desirable (perhaps as a basepoint example of such an asset). The legislation could also make provision to enable the types of asset specified to be amended by secondary legislation.

As an aside, the suggestion that a digital asset may be conceptualised as a specific transactional power over unique data entries on a blockchain ledger system (or as an exclusive power to make valid transactions on such a system), is an interesting and persuasive one at least for some types of digital assets. We also tentatively agree with the logic of treating a digital asset token and the underlying tokenised asset as two distinct assets or perhaps as digital twins.

We can foresee that the wide range of digital assets could create problems for legislation, as their varying characteristics might lead to different results depending on the circumstances. Consequently, formulating a definition and specifying particular rules to apply to all digital assets

may be troublesome. This is one argument in support of a relatively light-touch approach to legislation, whereby some general provisions are given for clarity but further detail and application in various contexts is left to the courts. Proceeding in this way also limits the ability for the law to impede innovation or fail to give legal effect to technological developments. Therefore, beyond the preceding and following suggestions regarding scope of legislation, great caution should be exercised to avoid being too prescriptive and detailed regarding how digital assets will work in the law.

Legislation should specify clearly that digital assets are property for the purposes of Scots law. The recognition of such assets as property is pivotal and will allow for them to be treated along with other property not only within property law itself, but in adjacent areas where digital assets are of relevance such as succession, family law, secured transactions, insolvency, diligence, trusts and delict. The express identification of digital assets as property should have this desired effect.

The legislation should probably specify the category of property within which digital assets are located. Our view is that they should be, in principle, identified in Scots law as a special type of incorporeal moveable property. They are not land or a right in relation to land and so are moveable property (rather than heritable property). While we note some of the similarities with corporeal moveable property identified in the consultation paper, we take the view that intangible property can be equated to incorporeal property in Scots law, and it may be counter-intuitive for digital assets to be corporeal moveables. We consider that tangibility/intangibility (almost always) determines whether property is to be corporeal or incorporeal respectively. Incorporeal moveable property is a relatively flexible category in Scots law (which avoids some of the categorisation difficulties in English law) and is not limited to claim rights which are transferred by assignation with intimation. Shares and intellectual property are examples of other forms of property within the category, and these are transferred using registration instead of intimation or assignation alone (for copyright). The “transfer” of digital assets on a ledger is not only analogous to delivery of corporeal moveables but may also be considered analogous to the mechanisms for transferring these other types of incorporeal moveable property. If digital assets are stated to be incorporeal moveable property, it should not be necessary to expressly state that they are not “goods” within the meaning of the Sale of Goods Act 1979, and, in any event, we agree that they are not goods, whichever broader category of property they fall into. In contrast to digital assets generally, however, some types of digital assets, such as stablecoins and Central Bank Digital Currencies, might require a different approach as they may be considered more akin to money.

It may be helpful if legislation could specify (albeit without focusing too much on one particular type of system) when the transfer of digital assets legally takes place. This may not be necessarily at the time or upon the event that transfer of digital assets technically takes place on the ledger. We agree that the usual property law principles governing derivative acquisition of ownership should apply to digital assets and the legislation could state this. We also agree that the recording of a transfer on the ledger would be a necessary step to transferring ownership of the assets but would not be sufficient to constitute an indefeasible title in the transferee as owner. We concur that the *nemo plus* principle should apply generally to digital assets meaning that the ledger may not be necessarily an accurate or complete record of the state of real rights in the digital asset shown there. The application of the principle could be captured in legislation. The identification of a distinction between ownership and practical control of a digital asset could be usefully included in legislation and the legislation might also identify the meaning and implications of digital control of digital assets. Control is a concept, with some variations, that is already familiar in relation to incorporeal moveable property in certain areas of commercial law.

Any plans for legislation in this area should take account of developments in English law with respect to the possibility of legislation there. Given the commercial nature of the topic and the likely cross-border elements that may exist, and to avoid additional intra-UK conflict of laws complications that may otherwise be created, a significant level of alignment with the English law position would be desirable. However, this is subject to the major caveat that the background Scots law within which digital assets are to function must be respected and accommodated. We therefore think that it would be very useful for the Expert Reference Group and/or the SLC to engage and promote close cooperation with the LCEW in the scope of the LCEW's ongoing project on Digital Assets, which is currently at the pre-consultation stage.

In a broader context on the private international law side, we are of the view that it would be preferable if private international law aspects of digital assets were considered under a separate initiative. We note that the LCEW announced the launch of its new project on Conflict of Laws and Emerging Technology in the first half of 2022 after its work on smart legal contracts, digital assets and electronic trade documents led to the identification of several private international law issues. We think that engagement and close cooperation between the Expert Reference Group and/or the SLC and LCEW in the scope of that project is also very important and should be promoted.