Law Commission
Reforming the law

# Digital assets in private international law: FAQs on the relationship with tax law, banking regulation, and the financial markets

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**This document has been prepared by members of the Commercial and Common Law team at the Law Commission. It has not been peer-reviewed by Commissioners and is not a formal Law Commission publication.**



This publication is available at https://lawcom.gov.uk/project/digital-assets-and-etds-in-private-international-law-which-court-which-law/.

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## BACKGROUND TO THIS PAPER

### Our work on private international law and digital assets

1.1 We began our work on digital assets and ETDs in private international law in 2023. We published a Call for Evidence in February 2024, which provided an introduction to private international law and the nature of the challenges that digitisation and decentralisation pose for this area of law. We are grateful to all those who submitted a response. The next formal stage of our project will be to publish a Consultation Paper with proposals for law reform.

1.2 Following the publication of our Call for Evidence, we became aware that a significant number of stakeholders seek clarity on how certain rules of private international law might apply in the wider legal context. Tax and banking regulation emerged as two core areas of concern. We also became aware that some issues surrounding digital assets used in certain commercial contexts, such as tokenised securities in the financial markets and linked assets, may benefit from a more detailed discussion.

1.3 We have therefore produced this document to explain in a little more detail how the approaches to digital assets taken by revenue authorities, regulatory bodies, and commercial practice may differ from the approach taken by private international law. The document is structured as a FAQs ("frequently asked questions") to respond directly to some of the most common concerns raised with us so far.

1.4 The following members of the Commercial and Common Law team have worked on this document: David Hertzell (senior counsel), Laura Burgoyne (team manager), Amy Held (lawyer). The document has not been peer reviewed by Commissioners and is not a formal publication of the Commission.

1.5 We welcome follow up questions arising from this document, which can be sent to conflictoflaws@lawcommission.gov.uk.

### Our previous work on digital assets

1.6 This project is the most recent in the Law Commission's work on emerging technology and private law. We have previously published on smart legal contracts, electronic trade documents (leading to the Electronic Trade Documents Act 2023), decentralised autonomous organisations ("DAOs") and, most relevantly for present purposes, digital assets.

1.7 In our work on digital assets, we concluded that crypto-tokens and certain other digital assets are capable of being objects of property rights under the private law of England and Wales. However, for the purposes of our work on private international law, it is important to recognise that these two streams of work are distinct. Private law and private international law are distinct legal disciplines, with distinct objectives and methodologies. For example, although private international law uses many terms also used in the substantive private law, such as "contract" and "property", it cannot be assumed that use of these terms in private international law reflect substantive definitions and concepts from private law.

1.8 From this, the challenges that digitisation poses for private international law significantly differ from those that they pose for the substantive law. It is of utmost importance in our project that these two areas of law are understood as conceptually distinct.

### Q.1. WHAT IS THE RELATIONSHIP BETWEEN PRIVATE INTERNATIONAL LAW AND OTHER AREAS OF LAW SUCH AS TAX LAW AND FINANCIAL SERVICES REGULATION?

1.9 A significant number of stakeholders have raised concerns as to how the "location" of a digital asset or crypto-token for the purposes of private international law relates to "location" for other legal purposes, notably tax and banking regulation. Many have said or assumed that there should be consistency across all legal areas on the question of "where" a digital asset or crypto-token is "located".

1.10 We recognise that many of the novel challenges that crypto-tokens pose for the law often seem to be asking the same question; one that essentially seems to relate to the geographical location of an object.

1.11 However, we do not think it helpful to think of these legal challenges simply in terms of asking "where" a crypto-token is "located". This is because thinking in these terms suggests that each legal discipline is asking the same question and for the same purposes. This in turn obscures the fact that different areas of law are underpinned by different objectives and policies that influence significantly both how the question is approached and the process of finding an answer.

1.12 Before exploring this in more depth, we think it would be helpful to begin by setting out some very basic differences as between different areas of law. For example:

(1) Private law. Private law concerns relationships between private parties (including individuals and businesses). Questions of property entitlements to a crypto-token is a matter of private law. So too are questions such as breach of contract or a duty of care in negligence.

(2) Private international law. Private international law is engaged where private law issues and relationships traverse national borders. Where the facts or issues of a private law dispute are international, private international law will be used to determine: (a) in which country's courts the parties should litigate their dispute; (b) which country's laws those courts should apply to resolve the dispute; and (c) how any judgment resulting from the litigation can be recognised and enforced in other countries. Broadly, private international law is concerned to identify which country's system of private law is most appropriate to govern any given cross-border private law issue. These questions are the focus of our current work.

(3) Public law. Public law is concerned with the actions and activities of public bodies. It includes, for example:

(a) Regulatory law. Regulatory law – such as financial services regulation or health and safety regulation – concerns the imposition of rights and duties in relation to particular conduct, the placing of restrictions on certain conduct (for example, that an activity may not be undertaken

without a licence) and the establishment and functioning of public bodies. It sets out the regulations and allows the relevant public body to enforce regulations, investigate breaches, and bring enforcement proceedings or prosecutions. Regulation is broadly a matter of public law. Whether domestic regulatory rules apply in an international or quasi-international context will depend on the terms of the regulatory rule itself. For example, depending on its drafting, a regulatory rule may apply only to activities carried on in England and Wales, or may apply more broadly, such as activities carried on by businesses having some operations, customers or effect in England and Wales.

(b) Criminal law. The starting principle in this jurisdiction is that the criminal law of England and Wales applies only to acts committed in England and Wales.[1] Where no part of the conduct takes place in England and Wales, a specific statutory provision is usually required for acts committed wholly outside the jurisdiction to enable prosecution here.[2] Typically, this will depend on either the act or the defendant having a particular connection with England and Wales (or the UK). There are a number of serious offences that can be prosecuted in England and Wales where the criminal act took place abroad, if the perpetrator is a UK national or habitually resident in the UK.

(c) Tax law. Taxes are imposed by public authorities on individuals, businesses and other entities. They are generally a matter for state governments. Tax law is often known as "revenue law".

(4) Public international law. Public international law broadly concerns relations between sovereign states and the operation of international organisations, such as the United Nations. Public international law encompasses a wide range of issues, such as international human rights, the conclusion of bilateral treaties between states, and the conduct of war. Public international law also includes rules that regulate the scope of each state's sovereign authority, including when that authority might extend beyond the state's territorial boundaries.[3] We consider these further below at paragraphs 1.19 to 1.23.

1.13 To a large extent, each of these areas of law are separate with their own rules, policies, and objectives. The extent to which these will influence how each area of law will respond to the question of "where" a crypto-token is "located" cannot be underestimated. We explore this, and why different areas of law may arrive at different answers, in more detail below.

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1 For offences covered by the Criminal Justice Act 1993, s 1 (generally economic offences such as theft, fraud, and blackmail), it is sufficient that any act or omission required to be proved took place in England and Wales. It is possible to prosecute fraud offences where all the relevant conduct takes place outside England and Wales if the result is a gain or loss which transpires in England and Wales: Criminal Justice Act 1993, s 2.

2 See eg the discussion in Intimate image abuse: a final report (2022) Law Com No 407, para 15.7.

3 See generally A Mills, "Private Law Regulation and Private Interests in Public International Law Jurisdiction" in S Allen et al, *The Oxford Handbook of Jurisdiction in International Law* (2019).

## Q.2. HOW IS *SITUS* RELEVANT FOR THE PURPOSES OF PRIVATE INTERNATIONAL LAW?

1.14 One of the most prevalent concerns raised with us relates to the rules of private international law that refer to the location of an object. These are the *forum rei sitae* and *lex rei sitae* rules ("court of the place where the object is situated" and "law of the place where the object is situated" respectively). These are often abbreviated to *forum situs* and *lex situs* ("court of the situation/location" and "law of the situation/location" respectively).

1.15 Identifying where an object is situated causes some challenges when applied to digital assets and other objects that do not occupy an obvious geographical location in the same way as conventional tangible objects. However, such challenges are not necessarily problematic for private international law, which has long developed techniques for dealing with objects that do not have an obvious physical location.

1.16 For example, patents are usually "localised" by reference to the register in which the relevant entitlements are maintained. Debts are usually "localised" by reference to the debtor. From this, it has become conventional in some parts of the private international law discourse to refer to the "artificial" or "juridical" *situs* of intangible objects, with expressions such as: "the artificial *situs* of a patent is the place where the relevant register is kept" or "the artificial *situs* of a debt is the place where the debtor is domiciled".

1.17 We recognise the intuitive appeal of such expressions. However, we consider that such expressions are unhelpful because they obscure the nature and ultimate objective of the exercise – which is to identify which country's system of private law is most appropriate to govern the cross-border private law issue arising from the object – and the policy considerations that this exercise engages. For this reason, phrases such as "artificial" or "juridical situs" have been criticised in both academic[4] and judicial contexts.[5] Many of these critiques argue for a more open analysis of the policy considerations that underpin these rules.

1.18 In the present context, such expressions are particularly unhelpful because they suggest that there can only be one single "place" where a digital asset can be "located" for legal purposes. To the extent that "place for legal purposes" is taken in private international law to mean the same thing as a purely geographical location, this is misleading. Whilst location within a particular territory remains a foundational principle of both private and public international laws, the allocation of sovereign authority as between states in any given case engages a nuanced analysis of a greater range of considerations.

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4 P Rogerson, "The Situs of Debts in the Conflict of Laws: Illogical, Unnecessary, and Misleading" (1990) 49(3) *Cambridge Law Journal* 441 to 460; A Held, "The Modern Property Situationship" (2024) 20(2) *Journal of Private International Law* 391. Amy Held was a member of the Advisory Panel until she joined the Law Commission specifically to work on this project as a law reform lawyer in November 2023.

5 *Raiffeisen Zentralbank Osterreich AG v Five Star General Trading LLC (The Mount I)* [2001] EWCA CIV 68, [2001] QB 825, [35], by Mance LJ.

1.19 To begin, public international law distinguishes between the types of acts that constitute an exercise of sovereign power. The main questions that arise in public international law are as follows:

(1) First, the question of when a person or set of facts may be subjected to the laws of a particular sovereign state. For example, must tourists comply with the laws of the foreign country to which they travel whilst on holiday there? And do they continue to be subject to the laws of the country where they usually live, even when they travel abroad? The application of a state's laws to a set of facts or person is an exercise of "prescriptive jurisdiction".

(2) Second, the question of when a sovereign state can exercise coercive power or control over persons or property. For example, when can a state commit a person to custody or seize their assets? Can a bailiff or other enforcement officer of England and Wales seize assets physically located in a foreign country? Committing a person to custody or seizing their assets is an exercise of "enforcement jurisdiction".

(3) Third, the question of when national courts may exercise judicial power. This is the exercise of "adjudicatory jurisdiction". It engages prescriptive jurisdiction insofar as a court will be applying the substantive law of a sovereign state to a set of facts. It also involves enforcement jurisdiction insofar as litigation usually results in a judgment that parties wish to enforce.

1.20 Different considerations underpin the exercise of each of these three types of sovereign acts. Although territoriality and geographical location do play a part, they are by no means determinative:

(1) Enforcement jurisdiction is strictly territorial: a state may only commit a person to custody or seize their assets when the person or assets are within the state's territorial boundaries.

(2) Prescriptive jurisdiction is less clear cut. The general rule is that the laws of a state apply within its territorial boundaries, but not generally outside them. However, what counts as "within the territorial boundaries" for these purposes is a complex question.[6] Many states also extend parts of their law, such as criminal law, extraterritorially to their nationals or residents, or on the basis of other accepted justifications.

(3) Adjudicatory jurisdiction is also less clear cut. In private law matters, the general rule of international jurisdiction is that the claimant must sue in the "home" court of the defendant. Most legal systems additionally admit grounds of jurisdiction based on other factors. Typically, what is required is an "adequate link" between the facts and issues of the case and state in whose court the claim is being litigated. In criminal matters, there is typically a stronger requirement that some

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6 Many states do commonly extend the application of their laws to events that might be considered to occur outside of the territorial borders, but which have significant effects within the territorial borders. This might include, for example, a price-fixing agreement made between companies outside of the territorial boundaries of a particular state, but which is aimed at harming the consumers within that state.

aspect of the criminal conduct took place within the territorial boundaries of state in whose court the offence is being prosecuted.

1.21 Adjudicatory jurisdiction helpfully illustrates that further distinctions may be made, depending on whether the exercise of sovereign authority is for private law, public law, criminal law, or tax law purposes. We consider these in more detail below in Question 3.

1.22 Here we note that these principles of public international law are mirrored in private international law: adjudicatory jurisdiction roughly corresponds with the "jurisdiction" question; prescriptive jurisdiction roughly corresponds with the "applicable law" question; and enforcement jurisdiction roughly corresponds with the recognition and enforcement of judgments. As such, even within private international law, different policy considerations underpin the rules of jurisdiction, applicable law, and the recognition and enforcement of judgments.

1.23 More importantly, each of these aspects of private international law take a different position as to the relevance and importance of geographical location. Where it is not possible to rely on purely physical factors to connect a legal issue – such as those arising from a crypto-token – with the private law system of a particular sovereign state, these policy considerations come to the fore.

1.24 As such, it is helpful to return to the basic methods and objectives of private international law, before examining the particular considerations that underpin the *forum situs* and *lex situs* rules.

### Q.2(a) What are the methods and objectives of private international law?

1.25 There are three main issues that must usually be resolved when questions of private international law arise, but in our project we are concerned in particular with the first two: jurisdiction and applicable law. For the reasons set out in paragraphs 1.19-1.23, it is worth repeating that we are concerned with jurisdiction and applicable law as two distinct aspects of modern private international law. These were treated separately in our Call for Evidence, and we summarise the relevant principles below.

1.26 There are two key factors that underpin the rules of international jurisdiction.[7] The first factor relates to the fairness and everyday practicalities of the litigation. This concerns both: (i) a wide range of issues that relate to the conduct of litigation itself; and (ii) justice in a more abstract sense, such as access to the courts to obtain an effective legal remedy. The second factor relates to the need for national courts to justify the assertion of sovereign authority in accepting jurisdiction over a claim if the claim also has links to the territories of other sovereign states.

1.27 By contrast, the traditional approach to applicable law is premised on the theoretical proposition that every legal issue that comes before a court "naturally belongs" to one

[7] T Hartley, "Basic Principles of Jurisdiction in Private International Law: The European Union, The United States and England" (2022) 71(1) *International and Comparative Law Quarterly* 213; A Held, "The Modern Property Situationship" (2024) 20(2) *Journal of Private International Law* 391.

country's legal system or another.[8] Many traditional applicable law rules therefore have taken the form of what is now known as a "fixed" applicable law rule: rules that prescribe simply and without more a single criterion for "connecting" a legal issue with the national legal system to which it "naturally belongs". As we will explain below, it is important to emphasise that the apparent simplicity of "naturally belongs" belies a wide range of complex policy considerations.

1.28 The *lex situs* rule is the paradigm example of a fixed applicable law rule: on its face, it prescribes simply and without any further criteria or considerations that property issues arising in a cross-border legal context are governed by the law of the place where the property object is situated. We discuss the policy considerations that underpin the *lex situs* rule in more detail below in Question 2(b).

1.29 In modern private international law, simple fixed rules are less common than they were in the past. In the USA, for example, there has been since the 1960s a move from fixed and rigid rules that "preselect" the applicable law for the court towards a more flexible "approach". This involves a court consulting a list of prescribed factors to consider when identifying the applicable law.[9] Such approach is often known as an "open-textured" rule.

1.30 The principle underpinning open-textured rules is recognised in the common law of England and Wales; both in the process of characterisation as well as in the application of the applicable law rules themselves.

1.31 For example, in *Mount Albert BC v Australasian Temperance and General Mutual Life Assurance Society Ltd*,[10] a case concerning the law applicable to certain contractual obligations, the Privy Council said the law of England and Wales has "refused to treat as conclusive rigid arbitrary criteria" the applicable law rules that prevailed at that time for contractual issues. Rather, the question of the law governing contractual obligations was a matter "to be ascertained in each case on a consideration of the terms of the contract, the situation of the parties and generally on all the surrounding factors".[11] Another example is *Raiffeisen Zentralbank v Five Star Trading LLC*,[12] a case concerning characterisation surrounding the assignment of a marine insurance policy. Here, the Court of Appeal said that the types of issues that the law recognises in the characterisation stage and the rules of applicable law to which they may lead are "man-made, not natural [and] have no inherent value, beyond their purpose in

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8 The theory was developed in the early 19th century by a prominent German jurist, Friedrich Carl von Savigny (1779-1861). The approach to the conflict of laws developed by Savigny remains highly influential.

9 Section 6 of the Second Restatement of the Conflict of Laws (1969) has been said to be an important example that enunciates the underlying ideology, and instructs the court to consider: (a) the needs of the interstate and international systems; (b) the relevant policies of the forum; (c) the relevant policies of other interested states and their interests in applying their law to the particular issue; (d) the protection of justified party expectations; (e) the basic policies underlying the particular field of law; (f) the objectives of certainty, predictability, and uniformity of result; and (g) the ease in determining and applying the governing law.

10 [1938] AC 224.

11 *Mount Albert BC v Australasian Temperance and General Mutual Life Assurance Society* Ltd [1938] AC 224, 240, by Lord Wright.

12 [2001] EWCA Civ 68, [2001] QB 825.

assisting to select the most appropriate law".[13] In this way, the "overall aim" has said to be "identifying the most appropriate law".

1.32 The ultimate objective underpinning an applicable law rule – simply to identify the most appropriate law to govern the issue at hand – is, in this way, far more obviously evident in an open-textured rule.

1.33 Many modern applicable law provisions alternatively use a combination of fixed and open-textured rules. The EU's Rome Regulations,[14] for example, often make use of the following structure:

(1) first, there is a general rule that applies as the default rule and points to a specific location;

(2) second, there are more specific rules that apply in specific circumstances that point to a specific location;

(3) third, there is an "escape clause" that applies if there is a country with which the particular issue is "manifestly more closely connected" than the places identified by the general and specific rules;

(4) finally, there may be a "catch-all" provision that applies when the applicable law cannot be determined using any of the other rules. In these circumstances, the approach taken by the rule mirrors the "escape clause" and the rule points to the place with which the issue is most closely connected.

1.34 By placing the fixed rules first as the default rules and treating the open-textured rule as a "last resort" to be applied in exceptional circumstances, the Rome Regulations tend to promote certainty over flexibility. In other legal systems, the emphasis is inverted: the open-textured rule is the general rule, and the fixed rules are merely indicative of the place that is, in specific circumstances, likely to be the place with which the case has its closest connection.[15]

1.35 We said, therefore, in our Call for Evidence that there is a variety of options available to us in relation to the formal design of any applicable law rule. Each pursues a different underlying policy. The basic decision as between the two extremes of a fixed rule and an open-textured rule has been said to rest ultimately on whether the emphasis is on:

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13 *Raiffeisen Zentralbank Osterreich AG v Five Star Trading LLC (The Mount I)* [2001] EWCA Civ 68, [2001] QB 825, [27], by Mance LJ.

14 The Rome I Regulation (EU) No 593/2008 is concerned with contractual obligations. The Rome II Regulation (EU) No 864/2007 deals with non-contractual obligations such as torts, product liability, and unjust enrichment claims. The Rome I and Rome II Regulations continue to have effect in England and Wales as assimilated law, subject to some minor amendments: see The Law Applicable to Contractual Obligations and Non-Contractual Obligations (Amendment etc) (EU Exit) Regulations 2019 (SI 2019 No 834).

15 See the example of the Japanese Act on the General Application of Law at para 6.150 to 6.151 in our Digital assets and ETDs in private international law: which court, which law? (2024) Law Commission Call for Evidence.

(1) prioritising certainty and foreseeability; meaning fixed rules which, if applied consistently, might not necessarily identify the most appropriate law in any given case by, for example, "caus[ing] hardship in the individual case"; or

(2) flexibility in applying the most appropriate law in every given case, thereby "ensuring justice in the individual case;" meaning "less predictable solutions overall".[16]

1.36 We repeat that, should it be necessary for us, in the course of our project, to propose a new applicable law rule, there are a range of considerations for us to bear in mind. We will need to be aware of the broad overriding objectives of the conflicts of laws, and the specific policy objectives pursued by the individual applicable law categories (such as contract and property).[17] We will need to consider the balance to be struck between predictability and certainty on the one hand, allowing parties to organise their affairs in advance; and flexibility on the other hand to allow for individual cases where the law identified by the general rule might not necessarily be the most appropriate. With this in mind, our options would include a combination of fixed and open-textured rules, one single open-textured rule, or many fixed but necessarily detailed rules.

1.37 If we consider a combination of fixed and open-textured rules is preferable, we will need to consider whether to start with a fixed rule that leads to an open-textured exceptional "escape clause"; or to start with an open-textured rule with presumptions for particular cases. Judicial experience in applying applicable law rules will be important in making these assessments.

1.38 In sum, private international law is broadly concerned with connecting a cross-border private law dispute to the courts and law of a particular country. Although physical location within a geographical territory plays a significant part in this process, this is only one factor amongst a range of other significant policy considerations. These considerations, moreover, differ as between the "jurisdiction" and "applicable law" question, as well as between different jurisdiction and applicable law categories.

### Q.2(b) What policy considerations underpin the private international law *situs* rules?

1.39 *Situs* (that is, the place where the object is situated) is a connecting factor that is usually associated with property disputes. Most, if not all, systems of private international law today use the *situs* as the primary connecting factor to identify the court in which a property dispute should be litigated and the law applicable to a property dispute.

1.40 The *situs* is, however, also sometimes used as a connecting factor for other types of issues. For example, section 72 of the Bills of Exchange Act 1882, as interpreted in accordance with section 2, uses the *situs* for the law applicable to certain contractual issues. The *situs* is also used in some of the rules for succession, matrimonial property, and insolvency issues. It is, therefore, particularly important to remain alert

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16 O Lando, "Contract" in K Zweigert and U Drobnig (eds), *International Encyclopaedia of Comparative Law (Vol III)* (1976) p 78, as cited in J Carruthers, *The Transfer of Property in the Conflict of Laws: Choice of Law Rules Concerning Inter Vivos Transfers of Property* (2005) para 9.05.

17 For example, we explain the differing policy considerations underpinning contract and property issues below from para 1.48 onwards.

to the different policy considerations that underpin use of the *situs* as a connecting factor in any rule of private international law.

1.41 Digital and decentralised objects pose unique challenges for the *situs* rules. However, the fact that these objects lack meaningful physical features is not inherently problematic for private international law.

1.42 As we said above, private international law has long developed recognised methods for dealing with such objects. We also said it is not always helpful to think of these methods as involving an "artificial" or "juridical" *situs*. Rather, it is preferable to think of the "localisation" exercise in terms of the objectives of private international law: to find some factor on the facts or issues of the case that convincingly connects the legal issue in dispute to the authority of a single sovereign state. In this, a wide range of considerations – physical, factual, and legal – may be taken into account. The fact that the object that has given rise to a dispute lacks obvious physical features is, therefore, not necessarily problematic for the case as a whole.

1.43 From this, additional considerations and objectives underpin the *forum situs* and *lex situs* rules for general property issues. These are, moreover, distinct to those that may underpin the rules for, say, contractual or tort/delict issues.

1.44 For jurisdiction, the *forum situs* rule tends to be underpinned by practical considerations relating to effective enforcement. Often, the "localisation" exercise turns on identifying the courts of the place where the object can be effectively dealt with for the purposes of particular remedies involving the object itself, such as delivery up of the object.[18] Thus, many rules of jurisdiction and the recognition and enforcement of judgments for property claims to movables refer to the courts of the place where the property object is located at the time of proceedings.[19]

1.45 For applicable law, the *lex situs* rule is used in several different contexts. The most obvious is for general property issues. For example, the question of priority as between competing claims to lumber[20] and a painting[21] was referred to the law of the place where the lumber and painting were situated at the time of the disputed acquisition. Similarly, priority as between competing negotiations of a bill of exchange is referred at common law to the *lex situs* rule.

1.46 Section 72 (as interpreted in accordance with section 2) of the Bills of Exchange Act 1882, however, also uses the location of a bill of exchange (at the time of delivery or of presentation) to identify the law applicable for certain contractual issues. These

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18 *Macmillan Inc v Bishopsgate Investment Trust Plc and Others (No. 3)* [1996] 1 WLR 387, 424; *Glencore International AG v Metro Trading International Inc (No.2)* [2001] 1 All ER (Comm) 103,[31], by Moore-Bick J. This rationale is also referred to in *Raiffeisen Zentralbank Osterreich AG v Five Star General Trading LLC (The Mount I)* [2001] EWCA Civ 68, [2001] QB 825, [36], by Mance LJ.

19 For the temporal specification in the rules for the recognition and enforcement of judgments, see eg section 4(2)(b) Foreign Judgments (Reciprocal Enforcement Act 1993 (UK); section 7(3)(b) Foreign Judgments Act 1991 (Australia); Article 22 quinquies (f) Ley Orgánica 6/1985, de 1 de julio, del Poder Judicial (Law of the Judiciary, Spain); s 517(1) Codigo Procesal Civil y Comercial de la Nacion (National Code of Civil and Commercial Procedure, Argentina).

20 *Cammell v Sewell* (1860) 5 H & N 728.

21 *Winkworth v Christie, Manson and Woods Ltd* [1980] Ch 496.

include the formal validity, interpretation, material validity, performance, and breach in relation to each of the contracts on a bill; as well as the holder's duties upon dishonour. Use of the *situs* in this context of negotiable instruments is often known as the *lex sitae cartae* rule ("law of the place where the charter is situated").

1.47 These different applications of the *situs* as a connecting factor in the general property and contractual contexts helpfully illustrate the importance of emphasising the role of policy considerations when a rule of private international law framed in terms of the location of an object must be applied in the digital and decentralised environment.

1.48 Here, bills of exchange are a particularly helpful example because it uses the same connecting factor – the location of the bill of exchange at the relevant time – for both contractual and property issues. In the electronic context with which we are concerned in our project, it might be tempting to think of the challenge as involving the "artificial" or "juridical" *situs* of an electronic bill of exchange. This tends to suggest there can only be one "place" where an electronic bill of exchange is or can be "situated" for legal purposes.

1.49 We think this approach is misguided because contractual issues and property issues engage very different policy considerations in determining very different legal issues:

(1) For contract, the ultimate issue might be determining the rights and obligations of the parties to the contract, or whether the contract is formally valid. To identify the most appropriate law to determine these issues, it would be appropriate to consider the policies that underpin contract law more broadly; such as freedom of contract,[22] the parties' intentions,[23] understandings,[24] reasonable expectations as commercial actors,[25] the nature of the obligations to be performed,[26] and the party incurring the obligation.[27]

(2) For property, the ultimate issue is usually determining which of two (usually innocent) parties' claim to entitlement should take priority. To identify the most appropriate law to determine this issue, it would be appropriate to consider the policies that underpin property law more broadly; such as certainty for third

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22 In most modern systems of private international law, the default rule for the law governing contractual obligations is the law chosen by the parties, eg Art 3(1) of the Rome I Regulation. For the development of party autonomy at common law, see Lord Collins of Mapesbury and J Harris (eds), Dicey, Morris & Collins, The Conflict of Laws (16th ed 2022) paras 32-003 onwards.

23 *Vita Food Products Inc v Unus Shipping Co Ltd* [1939] AC 277, 299 (PC).

24 *Mount Albert BC v Australasian Temperance and General Mutual Life Assurance Society Ltd* [1938] AC 224, 240, (PC) by Lord Wright.

25 *Enka Insaat Ve Sanayi AS v OOO Insurance Company Chubb* [2020] UKSC 38, [2020] 1 WLR 4117, [281], by Lord Sales.

26 Art 4(2) of the Rome I Regulation uses the "characteristic performance" of the contract (as well as the person obliged to perform) to identify the law governing a contractual obligation in the absence of a choice.

27 A Dickinson, "Electronic Trade Documents and the Conflict of Laws in the United Kingdom" [2024] *Lloyd's Maritime and Commercial Law Quarterly* 65, 66.

parties,[28] clarity,[29] commercial certainty and convenience,[30] and the sovereign authority to grant property rights.[31]

1.50 Given the diversity of policy considerations underpinning contractual and property issues, it may well be that these issues are referred ultimately to different applicable laws. Thinking in terms of the "artificial" or "juridical" *situs* of an electronic bill of exchange is therefore unhelpful because, if the language of "artificial *situs*" is taken too literally, it unhelpfully leads to the expectation that the "artificial *situs*" of an electronic bill of exchange will or should be the same place for contractual issues and property issues alike. In turn, this leads to the expectation that all legal issues – and not just contractual and property issues – should be governed by the same applicable law.

1.51 Moreover, these considerations only apply to questions of applicable law. For questions of jurisdiction, the policy considerations would be different again. Keeping with the bill of exchange as an example, disputes arising from bills of exchange will rarely concern a claim to the bill of exchange itself as an object of property rights.[32] Rather, they are far more likely to be contractual claims for payment. As such, dispute arising from bills of exchange will engage the rules of jurisdiction for contractual claims rather than property claims.

1.52 In sum, although applying the *forum situs* and *lex situs* rules to objects with no obvious physical location is frequently thought of as an exercise in physical "localisation", this is not helpful for the purposes of our project. It is far more productive to recognise that, even in the apparently simple cases of fixed rules for tangible assets, the private international law rules for property are underpinned by policy considerations. These, in turn, remain at the forefront of any analysis of how the traditional *forum* and *lex situs* rules might apply in the digital and decentralised contexts with which we are concerned in our project.

### Q.3. CAN THE PRIVATE INTERNATIONAL LAW *SITUS* RULES BE APPLIED IN THE PUBLIC LAW CONTEXT?

1.53 Many of our stakeholders have raised concerns regarding the approaches taken in private international law and other areas of law to the "location" of a digital asset. These have primarily been in relation to aspects of public law, such as revenue law and financial services regulation.

1.54 Again, we recognise that many of the novel challenges digital assets pose for the law often seem to be asking the same question "where is a digital asset located?" We repeat that we think it unhelpful to think of the challenges in these terms; and that it is

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28 *Winkworth v Christie, Manson and Woods Ltd* [1980] Ch 496, 509, by Slade J.

29 *Macmillan Inc v Bishopsgate Investment Trust Plc and Others (No. 3)* [1996] 1 WLR 387, 405.

30 *Macmillan Inc v Bishopsgate Investment Trust Plc and Others (No 3)* [1996] 1 WLR 387, 400A, by Staughton LJ.

31 *Glencore International AG v Metro Trading International Inc (No.2)* [2001] 1 All ER (Comm) 103, [31], by Moore-Bick J. This rationale is also referred to in *Raiffeisen Zentralbank Osterreich AG v Five Star General Trading LLC (The Mount I)* [2001] EWCA Civ 68, [2001] QB 825, [36], by Mance LJ.

32 We discuss this further at paragraph 1.109 and in Question 4(c) below.

preferable to consider the policies and objectives underpinning each individual area of law. This is because these policies and objectives influence how any individual area of law approaches the question and arrives at an answer. We therefore explored some of the basic policies and objectives that underpin various different areas of law above.

1.55 For private international law, we illustrated that the individual policies and objectives that underpin each of the rules of private international law mean that there is no single definitive answer to the question "where is a digital asset located?" It is therefore preferable to think in terms of asking: "what national system of private law is most appropriate to govern this particular legal issue that arises from cross-border dealings in a digital asset" or "in which national court should the parties litigate this private dispute arising from cross-border dealings in a digital asset?".

1.56 By contrast, in the public law context, the question of "where is a digital asset located" might more appropriately be reframed as "does this sovereign state assert public law authority over this act or event relating the digital asset?".

1.57 The policies that guide the answer to these questions differ significantly as between private law and public law contexts. From this, it is difficult to overstate the extent to which these differences play out in international law.

1.58 A very basic difference to note is that states take a far more unilateral approach to asserting their jurisdiction in public law matters than they do in private law matters. Unlike in private law matters, where the principle of comity between states has long been recognised at the international level,[33] states are generally less concerned in matters of public law to avoid conflicting or overlapping applications of their substantive laws. Areas that touch on public law are therefore more likely to include an element of extraterritorial reach. The application of US securities regulation[34] and anti-corruption legislation[35] to acts that occurred outside the territorial boundaries of the USA are both well-known examples of the US public law authorities unilaterally taking an extraterritorial approach to their substantive laws.

1.59 At the level of litigation, domestic courts will never apply the public law of a foreign country. In criminal, public, revenue, administrative, and even civil procedural law matters, courts will always apply their own domestic law. The courts of England and Wales will not apply the law of another country if doing so would enforce, directly or indirectly, a foreign penal law, a foreign revenue law, or other foreign public laws.[36]

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33 We discuss comity at para 6.107 to 6.110 of our Digital assets and ETDs in private international law: which court, which law? (2024) Law Commission Call for Evidence. We explained that it is one of the three core foundational principles of private international laws established in the seventeenth century, and we set out a modern definition formulated by reference to sovereignty and territoriality.

34 *Morrison v National Australia Bank* (2010) 561 US 247.

35 For example, the Foreign Corrupt Practices Act of 1977 (as amended) 15 USC §§ 78dd-1 onwards.

36 *Re State of Norway's Application (Nos 1 and 2)* [1990] 1 AC 723, 807 to 808. For further discussion, see A Briggs, *Civil Jurisdiction and Judgments* (7th ed 2021) para 21.10.

The fact that domestic national courts may apply the substantive law of another country is a distinctive feature of private law disputes.[37]

1.60 We discuss the specific policy considerations relating to tax, banking regulation, and financial services regulation below.

### Q.3(a) Can the private international law *situs* rules be applied in the tax context?

1.61 Many stakeholders referred to the position taken by HMRC, citing primarily the policy paper "Cryptoassets: Tax For the Individual"[38] with some further reference to the Decentralised Finance Taxation chapter of the Cryptoasset Manual 2021. Many stakeholders were of view that private international law and revenue law should take a consistent approach to the question of where a digital asset is located.

1.62 One particular concern was inheritance tax. We were told that, unlike capital gains tax, which has a statutory rule on location, [39] inheritance tax continues to rely on the common law in determining whether an asset is situated in the UK. Some stakeholders were of the view that, in the absence of a statutory rule, any analysis we undertake in our project could usefully provide guidance for a court setting a common law precedent in this inheritance tax context. Others were of the view that HMRC's position in relation to the location of a digital asset for the purposes of inheritance tax might be an alternative approach to international jurisdiction over property disputes to crypto-tokens.

1.63 We are unable to comment on any position taken by HMRC or any other revenue authority in relation to the "location" of a crypto-token or digital asset for tax purposes. Revenue law is guided by its own distinct policies, which must be considered on their own terms in any exercise undertaken by a revenue authority to determine the scope of its public law authority to levy taxes. These are, moreover, distinct to the policies that underpin the *forum* and *lex situs* rules, and private international law more broadly.

1.64 Although we are not in a position to comment on the policies that underpin revenue law, a very basic difference to note with private international law is the direct constitutional relationship between the individual and the state in the revenue law context. A revenue authority has considerable discretion in how it implements fiscal policies in the broader economic and public interests, subject only to broader constitutional considerations. Those subject to the revenue authority of a state cannot "opt-out" of any liability to pay tax. Attempts to evade tax may be prosecuted as a criminal offence.

1.65 We referred in our Call for Evidence to the continued use of nationality as a connecting factor in public international law and contrasted it with its general decline in private international law. There, we gave as an example the US system of taxation on the basis of nationality: all US citizens are liable to pay income tax to the US revenue

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37 A Mills, "Justifying and Challenging Territoriality" in R Banu, M S Green and R Michaels (eds), *Philosophical Foundations of Private International* Law (2024) p 182.

38 HMRC published this paper in 2018, which was followed by a policy paper for businesses in 2019. These papers no longer exist, having been incorporated into the Cryptoasset Manual published in 2021. Stakeholders should consult HMRC for the most up-to-date statements on cryptoasset taxation.

39 Section 275A Taxation of Chargeable Gains Act 1992. This does not include digital assets.

authorities, irrespective of where the income was earned, and where the US citizen is domiciled or habitually resident.[40]

1.66 Such approach of the US revenue authorities can cause considerable hardship for US citizens who live and work outside of the USA, who may be liable to pay tax in both the country where they work and the country of their nationality. In this way, the USA is an example of a state acting unilaterally in relation to its tax and fiscal policies: it will levy taxes without regard to the revenue laws of another state and the impact it may have on those who fall within the scope of their revenue laws.

1.67 From this, it is also worth noting that avoiding overlaps or conflicts between revenue laws is a matter of double taxation treaties, conclusion of which remains in the sovereign prerogatives of states. Here, public international law considerations, rather than private international law considerations, come to the fore.

1.68 For all these reasons, we do not consider that our project and the work of HMRC in relation to crypto-tokens overlap. Although private international law and revenue law may well seem to be concerned with the common question of "where is a crypto-token located?" it is important to look beyond this and think in terms of the policies that underpin each of private international law and revenue law.

1.69 Such differences in underlying policies lead to well-known divergences between private international law and revenue law in relation to domicile.[41] We consider the "location of a crypto-token" to be another area where private international law and revenue law may validly reach different conclusions on what appears to be the same or substantially similar question.

### Q.3(b) Can the private international law *situs* rules be applied in the banking regulation context?

1.70 We have become aware that the *lex situs* rule is often used by regulated entities in relation to their obligations under banking regulations.

1.71 For example, UK entities may be subject to foreign banking regulations that require crypto-tokens relating to foreign clients to be held "within" that foreign jurisdiction. We understand that, in order to comply, regulated entities often move a copy of the relevant server on which the relevant data is stored into that jurisdiction. We further understand that, as a result, the data may be "located" in several places: a primary server in one location, a back-up in another location, and a copy in the foreign jurisdiction. We are also aware that the *lex situs* rule is often used by regulated entities to determine the extent to which crypto-tokens accepted as collateral may be used for capital adequacy purposes. We understand that legal opinions on the enforceability of such collateral as a matter of private law are usually sought; and that

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40 Digital assets and ETDs in private international law: which court, which law? (2024) Law Commission Call for Evidence, para 3.37.

41 Domicile has different meanings for common law, statutory, and tax law purposes. We discuss the definitions of domicile at common law, under the Civil Jurisdiction and Judgments Act 1982, and Inheritance Tax Act 1984 from para 3.31 of our Digital assets and ETDs in private international law: which court, which law? (2024) Law Commission Call for Evidence. It is worth noting that considerations of domicile under the Inheritance Tax Act 1984 will largely be replaced by a 'long-term UK resident' test from 6 April 2025.

the *lex situs* rule is often used to identify the jurisdictions for which such legal opinions are to be obtained.

1.72 We appreciate the reasoning for use of the *lex situs* rule for these purposes; and recognise there is, on the face of it, a stronger relationship between property issues arising in the conflict of laws and such banking regulations than there is between property issues in the conflict of laws and revenue law. Even if all regulatory laws are essentially aspects of public law, both private law and banking regulation touch upon questions of private law entitlements.

1.73 Furthermore, some conflict of laws rules for property issues are designed specifically to further broader economic and regulatory objectives. Consider, for example, the EU's Settlement Finality Directive, which provides an applicable law rule for the rights of collateral security holders (within the meaning and scope of that Directive) in relation to securities "legally recorded on a register, account, or centralised deposit system".[42] Article 9(2) provides that where the register, account, or centralised deposit system is "located in a Member State", the law of that Member State will govern the rights and entitlements of collateral security holders.

1.74 One of the core policies underpinning the Settlement Finality Directive is reducing the legal and economic risks associated with participation in securities settlement systems.[43] This is made clear from the very first Recital, which refers to a Report to the Governors of the central banks of the G10 countries; [44] then notes the "important systemic risk inherent in payment systems which operate on the basis of several legal types of payment netting, in particular multilateral netting". From this, the "paramount importance" of the "reduction of legal risks associated with participation in real time gross settlement systems" is recognised.

1.75 Emphasis is further placed on circumstances where there is a close relationship between such systems and payments systems;[45] with the central banks of the Member States expressly named as participants in these systems to which the Directive will apply.[46] From this, further emphasis is placed on reducing systemic risk by ensuring the enforceability of collateral security[47] taken in relation to such securities on the insolvency of the collateral provider.[48]

1.76 Thus, the applicable law rule in Article 9(2) of the Settlement Finality Directive is intended to minimise systemic risk by providing legal certainty to both public and private participants in the settlement systems as to their rights as collateral holders. It is, however, critical to note that the supranational EU political and legal contexts in

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42 Article 9(2) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p. 45 to 50.

43 Recitals (1) and (2) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p 45 to 50.

44 The Lamfalussy report of 1990 to the Governors of the central banks of the Group of Ten Countries; Recital (1) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p 45 to 50.

45 Recital (2) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p 45 to 50.

46 Article 1(c) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p 45 to 50.

47 Recitals (9), (18), and (20) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p 45 to 50.

48 Recital (18) Settlement Finality Directive 98/26/EC, Official Journal L 166 of 11.6.1998 p 45 to 50.

which the Settlement Finality Directive – and other associated EU instruments[49] – were enacted differs considerably to the domestic and purely private international law context that we have been asked to consider.

1.77 It is not for us to propose or consult on rules of private international law that would further broader banking or other economic policies in the absence of a specific mandate and policy guidance from the relevant public bodies. This is because, again, although private international law and banking regulation may well seem to be concerned with the common question of "where is a crypto-token located?" it is important to look beyond this and think in terms of the policies that underpin each.

1.78 Nor is it for us to comment on the policies that underpin banking regulation. However, a very basic difference to note with private international law is the strong emphasis on financial stability and risk management in the context of banking regulation.

1.79 For example, in December 2023, the Basel Committee on Banking Supervision published a consultative document "Cryptoasset Standard Amendments".[50] In it, the Basel Committee decided not to propose changes that would bring cryptoassets that use permissionless blockchains within the "Group 1" asset class that qualifies for more favourable treatment under the relevant capital adequacy rules and credit mitigation schemes. Having conducted a review of the issue, the Basel Committee concluded that:

> use of permissionless blockchains gives rise to a number of unique risks, some of which cannot be sufficiently mitigated at present. Some of the most significant risks stem from the networks' reliance on third parties to carry out basic operations. Banks have limited ability to conduct due diligence and oversight over those third parties or prevent potential disruptions to the network. Similar analysis applies to political, policy, and legal risks, AML/CFT risks, and risks around settlement finality, privacy, and liquidity.[51]

1.80 These considerations are evidently quite different to the considerations that underpin private international law. In addition, a striking feature to note about banking regulation is that a simple decision such as that by the Basel Committee to exclude cryptoassets that use permissionless blockchains from certain regulatory schemes removes, at least for the time being, the possibility of using such cryptoassets for the purposes of these schemes. There is, in this way, a disjunct between the scope of credit mitigation schemes under banking regulations and the scope of private international law. From this, it would not be appropriate for the analysis in private

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49 The EU's Financial Collateral Directive built upon the "sound legal framework" for payment and securities settlement systems established by the Settlement Finality Directive to provide "further legal certainty" for the "provision of securities and cash as collateral" (Recitals 5 and 7) in a "Community Regime" (Recital 3). This was considered important for the "integration and cost-efficiency of the financial markets, as well as to the stability of the financial system in the Community, thereby supporting the freedom to provide services and the free movement of capital in the single market in financial services" (Recital 3). Article 9(1) provides that certain matters, as prescribed in Article 9(2), arising in relation to "book entry" securities will be governed by the law of the country in which the relevant account is maintained.

50 Basel Committee on Banking Supervision, *Cryptoasset Standard Amendments* (December 2023), https://www.bis.org/bcbs/publ/d567.htm (last visited 17 December 2024).

51 Above, p 1.

international law to be constrained by considerations that might well be decisive for banking regulation.

1.81 In any event, even if the Basel Committee or any national competent authority were to conclude that cryptoassets issued on a permissionless blockchain would qualify for favourable treatment under banking regulation, any question of compliance by regulated entities would be driven by the polices and considerations specific to banking regulation. As seen above, these remain distinct to those underpinning private international law.

1.82 From this, it is ultimately for banking regulation, rather than private law or private international law, to determine whether a copy of data relating to crypto-tokens moved into the relevant jurisdiction is sufficient for the purposes of any banking regulation that requires crypto-tokens to be "located within" that jurisdiction. Similarly, it is for banking regulation, rather than private law or private international law to determine whether a legal opinion based on the *lex situs* rule is sufficient for any credit mitigation scheme.

1.83 In sum, notwithstanding that both private international law and banking regulation touch upon private law entitlements, there remain significant differences in the policies underpinning the conflict of laws and banking regulation. Any purported exercise in the "localisation" of a crypto-token for each of these purposes should therefore be considered as engaging different legal questions.

### Q.3(c) How do financial services regulation and private international law interact?

1.84 We are aware of the need for certainty as to the future of the UK financial regulatory regime that will apply to cryptoassets and we are following the work of HM Treasury in this area.

1.85 It is, however, important to reiterate that private international law and financial services regulation are two distinct legal regimes. We repeat that our work on crypto-tokens in private international law therefore has no overlap with the existing regulatory regime or the regime for cryptoassets that HM Treasury is developing. In particular, where HM Treasury refers to the geographical scope of the future of UK financial regulation of cryptoassets, this refers to the scope of the regulatory regime and not the private law with which we are concerned.

1.86 As we have discussed above, there is more scope for extraterritorial reach of certain regulatory rules (for example, to capture activities carried out abroad but which have an impact in this jurisdiction) than there is for private law. As with overlaps and conflicts of the tax laws of different sovereign states, overlaps and conflicts between financial regulations is another area in which states are much more unilateral in asserting the application of their substantive laws. In EU financial regulation, for example, the European Commission may determine that the regulatory or supervisory regimes of certain non-EU countries are "equivalent" to the corresponding EU frameworks. Amongst other things, such recognition of equivalence reduces or eliminates the burden on entities regulated by the non-EU country of overlapping compliance obligations should they seek to enter the EU markets. Critically, however, decisions on equivalence are taken unilaterally by the EU; that is, without, for example, regard to any reciprocal recognition of equivalence or otherwise by the

foreign country in question or the effect on the regulated entities. The UK has a similar regime.

1.87 Several stakeholders nevertheless raised concerns about friction, competition, or overlap between financial services regulation and private international law. Some were concerned that the way in which private international law approaches the issue of *situs* might bring market participants within the regulatory perimeter. There was accordingly support for a consistent approach to the scope of national financial services regulation and applicable law.

1.88 We do not consider that there is any overlap between our project and the operation of any national financial services regulatory regime. Again, we do not presume to comment on the policies that underpin financial services regulation. However, a very basic difference to note with private international law is the strong emphasis on conduct and consumer protection.

1.89 From this, a single transaction or financial service will be viewed by financial services regulation and private law through very different lenses. A financial services regulator might view a staking transaction with a keen eye on what the staking service provider must disclose to potential clients and how it should keep its records. That same staking transaction viewed from the perspective of private law might focus more on who is entitled to the staked crypto-token or who is entitled to any profits.

1.90 We are not aware of any areas of financial services regulation where the financial asset or product itself is the subject of regulation; rather, financial services regulation is directed at specified activities (including activities in respect of any crypto-tokens that comprise "specified investments")[52]. Nor are we aware of any circumstances in which a financial transaction, service, or conduct falls within the regulatory perimeter simply on the basis that a financial asset or product is "located" within the territorial boundaries of England and Wales.

1.91 We reiterate again that our work has no bearing on regulatory permissions or obligations required under the regulatory regime.

### Q.4. HOW DOES CHARACTERISATION WORK IN COMMERCIAL AND FINANCIAL MARKETS USE CASES OF DLT?

1.92 Since publishing our Call for Evidence, a significant number of stakeholders have expressed the concern that we did not sufficiently distinguish between digital assets that are the focus in themselves as objects of property rights, and digital assets that are incidental to use of distributed ledger technology ("DLT") as a record or ledger. They explained that in the financial markets, most applications of DLT do not purport to create a digital asset with inherent value in itself as an object of property rights, but are intended to represent or evidence rights in relation to registered securities. The technology is leveraged specifically for use as a "mere" ledger or record of the rights and entitlements.

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[52] See eg Financial Conduct Authority, *Guidance on Cryptoassets, Feedback and Final Guidance to CP 19/3* Policy Statement PS19/22 (July 2019), from p 40, https://www.fca.org.uk/publication/policy/ps19-22.pdf (last visited 17 December 2024).

1.93 We deliberately did not make this or any other distinction between different use cases explicitly in our Call for Evidence. This is because we thought that structuring our project by reference to particular use cases might result in a fragmented discussion of the underlying issues insofar as they are relevant and problematic for private international law. Rather, our approach was to emphasise how these differences would be considered and resolved by the characterisation stage of the traditional conflict of laws analysis. In other words, we emphasised that the conflict of laws is often less immediately concerned what the asset or object "is" and tends rather to focus on the nature of the dispute that has arisen in relation to it.

1.94 From this, we have come to recognise that the nature and relevance of the characterisation process as a question distinct from what an object "is" can easily be – and often is – obscured by expressions such as "the law governing digital assets" or "the law applicable to digital assets". We said in our recent "ETDs in private international law: FAQs" that, although such expressions are prevalent in both the market and in the academic discourse, they are both unhelpful and misleading. Such expressions tend to suggest that the conflict of laws rules apply to specific types of *objects*, such as a piece of paper, a painting, or a car. This is not entirely accurate. Rather, the conflict of laws rules apply to the various rights, obligations, and relationships that arise from dealings in an object.

1.95 We therefore think we think it is worth discussing in more detail the distinction between objects in private law, and the conflict of laws process of characterisation. We also discuss how these principles might be relevant for use of DLT in the financial markets and in relation to linked assets.

### Q.4(a) Why is it unhelpful to think in terms of "the law applicable to the digital asset"?

1.96 Novel objects such as crypto-tokens pose novel problems for the law. It is, however, important to remember that the challenges posed for private international law are different to the challenges posed for substantive private law.

1.97 From this, it is important to distinguish two core questions arising in two different contexts:

(1) Private law: How should a novel object be conceptualised for private law purposes? Or in other words, what "is" a crypto-token in law and what types of legal rights might a person have in relation to a crypto-token? This is a substantive private law question with which we are not concerned in our present project on private international law, but which we considered in our digital assets project. There we concluded that crypto-tokens can constitute objects of property rights.

(2) Private international law: What is the nature of the particular legal issue that falls to be analysed for the purposes of the conflict of laws? Or in other words: what is the real nature of the issue in dispute between the parties to cross-border litigation? This is the question of characterisation, which is a core aspect of our project.

1.98 Evidently, the two questions are to some extent interrelated: the nature of an object gives some indication of the issues that may arise in relation to it; and the issues that

may arise in a dispute may be so characteristic of a particular type of object that, over time, the issue and object are recognised as forming a legal "unit" in a special rule.[53] Accordingly, it has been said that, ideally, substantive conceptualisation in private law should precede the issues that arise in private international law. A robust conceptualisation of legal form not only informs and opens up the range of potential connecting factors,[54] but it also informs the process of characterisation.[55]

1.99 Nevertheless, it is important to recognise that these two questions are conceptually distinct. Critically, it is important to note that uncertainty in the private law surrounding questions of conceptualisation does not necessarily preclude an analysis in private international law. This is particularly important to keep in mind in areas where the law is still uncertain or developing, such as the digital and decentralised contexts with which we are concerned in our project.

1.100 To illustrate these points, consider crypto-tokens in a permissionless DLT network. These could be conceptualised at the substantive level in various different ways. Depending on the aspect on which the conceptualisation focuses, the conclusions in substantive law and private international law may differ considerably.

(1) Emphasis on the network aspect of a crypto-token in a permissionless DLT network may lead to conceptualisation as a series of contracts between participants.[56] The result in private international law is that disputes in relation to the crypto-tokens, as a species of intangible property arising by reason of participation in the network, would be characterised as a contractual matter within the scope of the Rome I Regulation.[57]

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53 Land/immovables, for example, attracts many unique considerations in substantive law that have implications in private international law, particularly at the characterisation stage. On the rule that characterisation in property matters departs from the *lex fori* and is, instead, governed by the *lex situs*, see Lord Collins of Mapesbury and J Harris (eds), Dicey, Morris & Collins, The Conflict of Laws (16th ed 2022) para 23-002 onwards, especially para 23-009; and A Held, "The Modern Property Situationship" (2024) 20(2) *Journal of Private International Law* 391, pp 423 to 424.

54 A Held, "Crypto Assets and Decentralised Ledgers: Does *Situs* Actually Matter?" in A Bonomi, M Lehmann and S Lalani (eds), *Blockchain and Private International Law* (2023) p 257.

55 A Held, "Crypto Assets and Decentralised Ledgers: Does *Situs* Actually Matter?" in A Bonomi, M Lehmann and S Lalani (eds), *Blockchain and Private International Law* (2023) p 216.

56 A Dickinson, "Cryptocurrencies and the Conflict of Laws" in D Fox and S Green (eds), *Cryptocurrencies in Public and Private Law* (2019) para 5.109.

57 Above. It is important to emphasise, however, that this particular analysis applies only to the rights and obligations as between participants to the network. Professor Dickinson distinguishes such internal rights from those arising outside of the network. These transactions outside of the network would be characterised differently and would attract the application of other applicable law rules.

Dr Burcu Yüksel Ripley sets out a similar conceptualisation, albeit for transfers of cryptocurrencies taking place within permissioned networks only. Dr Yüksel Ripley concludes that the result in private international law is that any disputes would be characterised as a contractual matter within the general rule under the Rome I Regulation, and in the absence of a choice of law, within the scope of Article 4(1)(h): B Yüksel Ripley, "Cryptocurrencies Transfers in Distributed Ledger Technology-Based Systems and their Characterisation in Conflict of Laws" in J Borg-Barthet, K Trimmings, B Yüksel Ripley and P Zivkovic (eds), *From Theory to Practice in Private International Law: Gedächtnisschrift for Professor Jonathan Fitchen* (2024) pp 117 to 122.

(2) Emphasis on the network aspect of a crypto-token in a permissionless DLT network may lead to conceptualisation as a series of multilateral contracts between participants within the legal concept of an unincorporated association. The result in private international law is that any dispute in relation to the crypto-tokens would be characterised as a contractual matter excluded from the scope of the Rome I Regulation under Article 1(2)(f).[58]

(3) Emphasis on the distributed ledger aspect of a crypto-token in a permissionless DLT network may lead to a conceptualisation as a registered asset where the decentralised ledger functions as a register of entitlements.[59] The result in private international law is that any dispute in relation to the crypto-tokens would be characterised as a property matter to which the *lex situs* rule applies, with the register coming to the fore as a connecting factor.[60]

(4) Emphasis on the private key aspect of a crypto-token in a permissionless DLT network may lead to a conceptualisation as an asset functionally comparable to a corporeal movable where the private key functions in a manner akin to possession.[61] The result in private international law is that any dispute in relation to the crypto-tokens would be characterised as a property matter to which the *lex situs* rule applies, with the functional equivalent of control coming to the fore as a connecting factor.[62]

1.101 The issues of characterisation are in this way particularly complex in our project, given that DLT and crypto-tokens are used in a wide variety of ways in different commercial contexts and for different purposes. We consider below how characterisation might work in relation to applications of DLT in the financial markets and in relation to "linked assets".

### Q.4(b) How might characterisation work in the financial markets?

1.102 We think that the concern raised by stakeholders in relation to digital assets used in the financial markets (mentioned above in paragraph 1.92) represent use cases where the substantive conceptualisation ought to emphasise the distributed ledger aspect of the technology, rather than the private key or the token as an asset in its own right.

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58 A Held, "Private Keys and Blockchains: what *is* a Cryptoasset in Law?" (2020) 35(4) *Butterworths Journal of Banking and Financial Law* 250.

59 Hin Liu sets this conceptualisation in substance, albeit as one of two possibilities for a blockchain security where the crypto-token is linked to the payment obligation of the issuer: H Liu, "The Legal Nature of Blockchain Securities" [2021] *Lloyd's Maritime and Commercial Law Quarterly* 476 to 502 generally (490 to 494 in particular).

60 A Held, "Private Keys and Blockchains: what is a Cryptoasset in Law?" (2020) 35(4) *Butterworths Journal of Banking and Financial Law*; A Held, "Finality, Rights *in Rem*, and the Blockchain: Can Transactions in Cryptoassets be Set Aside?" in M Lehmann and C Koller (eds), *Digital Assets in Enforcement and Insolvency* (Hart, 2025) p 278 to 282.

61 See n 59 above, 476 to 502 generally (482 to 489 in particular). Hin Liu sets out this conceptualisation in substance, albeit as one of two possibilities for a blockchain security where the crypto-token is linked to the payment obligation of the issuer.

62 A Held, "Finality, Rights *in Rem*, and the Blockchain: Can Transactions in Cryptoassets be Set Aside?" in M Lehmann and C Koller (eds), *Digital Assets in Enforcement and Insolvency* (Hart 2025) p 275 to 278.

1.103 As we have said, this will likely lead to a characterisation in private international law that emphasises the distributed ledger as a register or record of entitlements to some asset. Current financial markets law and practice shows the prevalence of registers and records that are used in some way to determine rights in relation to financial assets. These include, for example, the "issuer register" and "operator register" for UK company shares in direct holding models, and the "book entry" records of a financial intermediary, depository, or custodian for intermediated holding models. As a matter of substantive law, these registers and records are subject to different legal rules and regulatory regimes.

1.104 In private international law, however, the general rule is that such assets are "situate" at the place where the register is kept or the record is maintained. In the terms of policy considerations that we consider more helpful for our purposes, private international law is generally concerned to identify the place where updates to the register or record are effected. This is in line with the general policy underpinning the rules of private international law for property issues: property rights in relation to objects that do not have any obvious physical location are often said to be "situate" in the country where they are properly recoverable or can be enforced.[63]

1.105 Thus, in *Macmillan Inc v Bishopsgate Investment Trust Plc (No 3)*,[64] a case concerning shares, the Court of Appeal said that shares are "situate" in the country where, under the law of the country in which the company was incorporated, they can be effectively dealt with as between the owner for the time being and the company. From this, if the law of the place where the company is incorporated provides that shares can only be transferred by registration on a particular register, property issues in relation to the shares will be determined by the law of the place where the register is kept.

1.106 The EU Directives on certain proprietary issues arising from securities held in the settlements systems are underpinned by a similar approach. Article 9(2) of the Settlement Finality Directive provides that the rights of collateral holders arising from securities "legally recorded in a register, account, or centralised deposit system located in a Member State will be governed by the law of that Member State." Article 9(1) of the Financial Collateral Directive provides that certain proprietary issues arising from book entry securities provided as collateral (as prescribed in Article 9(2)) will be governed by the law of the place where the "relevant account is maintained".

1.107 We recognise that such commercial emphasis on the distributed ledger aspect of DLT in certain use cases is inconsistent with expressions such as "the law governing the digital asset" or "the law applicable to the digital asset". As we have said above, such expressions are misleading because they focus on the asset itself, whereas the conflict of laws rules apply to the rights, obligations, and relationships to which dealings with an asset give rise.

1.108 That said, we also repeat that what an object "is" for private law purposes does often have a significant bearing on the types of rights, obligations, and relationships that

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63 Lord Collins of Mapesbury and J Harris (eds), Dicey, Morris & Collins, The Conflict of Laws (16th ed 2022) Rule 136(1).

64 [1995] EWCA Civ 55; [1996] 1 WLR 387 (CA).

arise from the dealings in that object. This in turn has a significant bearing on the types of issues that that courts will be called upon to characterise in any conflict of laws analysis.

1.109 To illustrate, we think it useful to consider DLT as being capable of creating a digital object that is functionally akin to a piece of paper. A piece of paper is obviously an object recognised by the law. However, there is no one singular private law treatment of pieces of paper; nor one singular conflict of laws rule that applies "to a piece of paper". How a piece of paper is used leads to very different types of treatment in private law, which then influences the types of issues that might be subjected to a conflict of laws analysis in cross-border litigation before the courts. We give some examples below.

(1) A photograph is simply a piece of paper. However, a particular photograph may have such personal value that a person may be prepared to bring a claim in negligence or trespass to goods in relation to any damage done to the photograph by a third party. In private international law, such claims would fall to be characterised by the courts of England and Wales an issue relating to torts. The photographer will also have copyright in the photograph that will be protected under intellectual property law. In private international law, the four main issues that arise in relation to intellectual property rights[65] are referred to different laws, including the *lex loci protectionis* ("law of the place where protection is sought"), the *lex situs*, and the *lex loci delicti commissi* ("law of the place where the wrongful act of infringement was committed").

(2) The four original copies of Magna Carta are simply pieces of paper (or the historic equivalents of parchment or vellum). However, the original copies of Magna Carta have such cultural importance that they do not fall under the general rules of private law. Many legal systems recognise a special class of objects called *res extra commercium* ("things outside of commerce") that are excluded from the ordinary rules of private property law on the basis that they are of significant public importance. Thus, in England and Wales, there are special rules that determine whether what might otherwise be an "ordinary chattel" is removed from the ordinary rules of personal property as a "cultural object", and from there, whether a "cultural object" is a "national treasure".[66] In private international law, the general rules that apply to property issues may be affected by specific rules that apply to cultural property in cross-border circumstances, for example, when the cultural object is loaned legally for the purposes of an exhibition or has been looted in times of war.[67]

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65 These are validity, infringement, initial ownership, and transfer.

66 See the Waverley Criteria, e.g., para 12 of https://www.artscouncil.org.uk/sites/default/files/download-file/Export_criteria_March_2015.pdf (last visited 17 December 2024).

67 On the law applicable to cultural property, as cited in Lord Collins of Mapesbury and J Harris (eds), Dicey, Morris & Collins, The Conflict of Laws (16th ed 2022) para 25-009, see M Frigo, "Circulation des biens culturels, détermination de la loi applicable et méthodes de règlement des litiges" (2015) 375 *Recueil des Cours* 89; Roodt, *Private International Law, Art and Cultural Heritage* (2015); M-A Renold, "Legal Obstacles to Claims for the Restitution of Looted Art" (2017/2018) 19 *Yearbook of Private International Law*. 247; A Chechi, "When Private International Law Meets Cultural Heritage Law – Problems and Prospects"

(3) A banknote of the Bank of England is simply a piece of paper (or the modern-day equivalent of polymer). However, the public and commercial functions of banknotes issued by the Bank of England are such that they are subject to various different private and public law regimes. UK banknotes have their origin in negotiable instruments law as the promissory notes issued by the Bank of England to pay the bearer a certain sum of gold.[68] From this, these promissory notes gained special status in England and Wales as legal tender and "money". Accordingly, in private law, banknotes of the Bank of England are an exception to the *nemo dat* rule that applies to ordinary chattels (that is, that a transferor can confer no better title to a transferee than the transferor themself has).[69] In private international law, banknotes recognised as legal tender give rise to a variety of issues that are referred to a wide range of rules. These include the *lex situs*, the *lex monetae* ("law of the issuing sovereign monetary authority"), the *lex loci solutionis* ("law of the place where the monetary obligation is to be performed"), and the *lex obligationis* ("law of the monetary obligation").[70]

(4) A global note held by the Bank of New York Mellon as common depository for Clearstream and Euroclear is simply a piece of paper. However, the commercial function of a global note and the way in which interests in it are traded within the modern financial markets infrastructure means that it is highly unlikely to form the object of a private law dispute as a distinct object of property rights. In private international law, debt obligations issued in global note form give rise to a variety of legal issues that are referred to a wide range of applicable law rules. Property issues are often tailored to the structure of the intermediated system of holding securities, such as the "place of the relevant intermediary account"[71] and the law "expressly agreed in the account agreement".[72]

(5) A paper bill of exchange is simply a piece of paper. However, the commercial functions of a bill of exchange within a very particular framework of interconnected contractual rights, liabilities, and obligations mean it is also unlikely to form the object of a private law dispute as an object of property rights. In private international law, the main rules for legal issues arising from bills of exchange address contractual issues, such as those set out in section 72 of the Bills of Exchange Act 1882. Issues of priority as between competing indorsements are usually referred to the *lex cartae sitae*.

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(2017/2018) 19 *Yearbook of Private International Law* 269; European Parliament Report, *Cross-Border Restitution Claims of Looted Works of Art and Cultural Goods* (November 2017).

68 Such promise is still printed on the face of banknotes issued by the Bank of England, but these can no longer be exchanged for gold. Rather, banknotes can only be exchanged for other Bank of England banknotes of the same face value.

69 *Miller v Race* [1758] 1 Burr 452; *Lipkin Gorman v Karpnale Ltd* [1991] 2 AC 548.

70 See generally E Prevost "The Law Applicable to Legal Tender of the Digital Euro: the End of the Conundrum?" (2024) 11 *Butterworths Journal of International Banking and Financial Law* 685.

71 Article 9 Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements (Financial Collateral Directive) Official Journal L 168 of 27.6.2002 p 43–5.

72 Article 4 of the Convention of 5 July 2006 on the Law Applicable to Certain Rights in Respect of Securities held with an Intermediary (2006 Hague Securities Convention).

(6) A paper share transfer instrument is simply a piece of paper. However, although a duly completed share transfer instrument has considerable significance in the transfer of shares from one person to another, its significance in relation to membership in a company (and, therefore, "ownership" of the shares) is limited. Typically, membership depends on registration in the register of members.[73] It is, therefore, highly unlikely that a share transfer form itself will form the object of a private law dispute as an object of property rights. In private international law, the rules relating to company matters are referred to the law of the place where the company is incorporated. If, according to this law, shares can only be transferred on a particular register, property issues in relation to the shares will be governed by the law of the place where the register is kept.[74]

1.110 From this, although it is often intuitive or convenient to think of piece of paper as an object or "thing" for which there is a particular conflict of laws rule, the question "what law applies to/governs a piece of paper" is unhelpful in a conflict of laws analysis.[75] At most, this can be taken as shorthand for "what various different laws are applicable to the various different legal issues arising from dealings in various different uses of pieces of paper". Moreover, each particular piece of paper will have associated with it a vast range of different conflict of laws rules for each of the various legal issues that might arise from dealings in that paper. The way in which the paper is being used will, therefore, in practice have a significant bearing on the types of issues that might come to be subjected to an analysis in characterisation by the courts.

1.111 All of the foregoing analysis in relation to pieces of paper may be applied to digital assets and crypto-tokens. Just as there is no singular private law treatment of a piece of paper, there is no singular private law treatment of a digital asset or crypto-token. From this, there is no singular applicable law rule that applies "to a digital asset" or that "governs a crypto-token".

1.112 Private international law is, however, well-equipped with the process of characterisation to recognise that dealings in digital assets and crypto-tokens give rise to a wide range of rights, obligations, and legal relationships, depending on how they are used. Where DLT is used primarily to create a record of entitlements, we expect that the significant authorities on registered assets and/or assets that otherwise rely on a record to determine entitlements would be duly considered should the proper characterisation be put in issue before the courts.

1.113 We do not think there would be any new and novel challenge in applying these applicable law rules where the relevant blockchain ledger or record of entitlements is

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73 Under section 768(1) of the Companies Act 2006, share certificates are *prima facie* evidence of title to shares; and the new issue of bearer shares is now prohibited in the UK under section 779(4) of the Companies Act 2006, as amended by section 84 of the Small Business, Enterprise, and Employment Act 2015.

74 *Macmillan Inc v Bishopsgate Investment Trust Plc (No 3)* [1995] EWCA Civ 55; [1996] 1 WLR 387 (CA). It is worth noting that, although the Court was divided on this issue, the alternative of the law of the place where the company is incorporated would pose little difficulty in the digital or decentralised context with which we are concerned.

75 It is worth noting that in some jurisdictions, particularly those based in Germanic legal traditions, this terminology is somewhat more prevalent. It is, however, important to note that such terminology reflects significant differences in private law theory and has no application in the law of England and Wales.

maintained or operated by a central entity. The presence of any such central operator who reserves to itself the authority to admit participants to the network or commit updates to the ledger is a strong connecting factor that would be of significant weight in any conflict of laws analysis.[76] In our Call for Evidence, we suggested that most applications of DLT in the traditional financial markets were likely to be permissioned systems. This was confirmed in all responses to our Call for Evidence submitted by stakeholders active in the financial markets.

1.114 The position is different where the distributed ledger is indeed operated on a wholly decentralised basis, that is, with no one entity occupying a hierarchical position of authority and the authority to commit updates to the ledger is, instead, dispersed amongst nodes that may be anywhere in the world. Here, however, the challenges posed to private international law are essentially the same as they are in relation to the situation on which we focussed in our Call for Evidence: a wholly decentralised crypto-token held directly without any intermediaries. To a large extent, focussing on either the ledger or on the token are simply two sides of the same coin. We noted in our Call for Evidence and again above at paragraph 1.100 the possibility of "localising" a crypto-token by reference to the ledger.

1.115 Were the analysis to focus, however, on the distributed ledger aspect of any wholly decentralised and permissionless application of DLT, the commercial context in which the record is being used would not necessarily hold any significant weight for the purposes of a private international law analysis. A wholly decentralised record of trading in a security in the financial markets and a wholly decentralised record of indorsements on an electronic negotiable instrument give rise to the same problem in private international law. This is the fact that, owing to the absence of a single master copy of the record or any central entity responsible for maintaining the record, there is no one single place where the register is "kept" or the record "maintained". If the register is "kept" or the record is "maintained" literally "nowhere and everywhere at the same time", identifying the most appropriate law to govern property entitlements to the relevant asset becomes a significant challenge.

1.116 We recognise that our decision not to refer to individual use cases of DLT may have given the impression that we are not aware that applications differ considerably in current commercial practice. However, given the emphasis in our project on private international law as a distinct legal discipline with its own particular methodology, we prefer to address these differences by emphasising the importance of characterisation.

1.117 Ultimately, the challenges for private international law with which we are concerned remain consistent, irrespective of whether the object of the private international law analysis "is" a wholly decentralised crypto-token (such as bitcoin held directly) or "is" an entry or entries in a wholly decentralised ledger (such as the blockchain on which entitlements to bitcoin as amongst the nodes are recorded). That said, private international law is well equipped to distinguish between use cases through

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[76] See, for example, the issue of data sharding, cloud storage, and the significance of cloud service providers from para 3.68 onwards of our Digital assets and ETDs in private international law: which court, which law? (2024) Law Commission Call for Evidence. In para 3.93, we discuss the significance of the cloud service provider in relation to data stored in the cloud as shards in direct comparison with data recorded on a wholly decentralised ledger.

characterisation: in the former case, the issue might be characterised as a property claim arising from the crypto-token itself as an object of property rights; in the latter case, the issue might be characterised as the validity or priority of entries on the (blockchain) register or ledger.

1.118 Finally, we reiterate that our work does not touch upon regulatory permissions or requirements that regulate the manner in which financial assets must be recorded or registered, such as under the Companies Act 2006 or the Uncertificated Securities Regulations 2001. Whether or not UK company shares or debentures, particularly in the direct holding models, may legally be issued or recorded using DLT remains a matter for regulation, not private international law.

### Q.4(c) How might characterisation work in the context of "linked assets"?

1.119 We did not address linked assets specifically in our Call for Evidence. However, we are aware there are some concerns relating to various issues surrounding linked assets, which we address briefly below.

1.120 As a general starting point, there are significant parallels between linked assets and the law of negotiable instruments: both involve a right that is considered to be "represented by" or "locked up in" a piece or paper or modern-day token equivalent. Conceptually, there is little to distinguish a bearer bill of lading that represents rights against the carrier in relation to the cargo, and a token that purports to represent rights that are "linked" to that cargo. In both cases, transfer of the bearer bill of lading and transfer of the token purports to transfer rights in relation to the cargo.

1.121 Most linked assets in the crypto-token sphere are offered by a clearly identified person, usually referred to as the "issuer", pursuant to some form of contractual arrangement. In many cases, these contractual arrangements expressly provide that the issuer warrants that the underlying or "linked" real world asset is kept safe in the issuer's custody; and that the token represents a right against the issuer to redeem that underlying asset. Some also expressly confirm that the token does not represent property rights in the underlying asset itself, but a right against the issuer to redeem the underlying asset.[77]

1.122 For example, a non-fungible token ("NFT") might be issued by an entity that "represents" the right to redeem a particular rare bottle of whisky, which is kept in the safe custody of the issuer. The issuer undertakes to exchange the bottle of whisky upon the demand and presentation of the NFT, which is then "burned". Until redemption, the NFT can be bought and sold. Ultimately, the issuer will deliver the bottle upon request by the current holder of the NFT.

1.123 Linked assets are often said to give rise to three distinct issues: the law "governing the linked asset", the law "governing the link", and the law "governing the token". We take each in turn.

1.124 The question of the law "governing the linked asset" is the most straightforward, even if the question is inappropriately phrased. For the reasons we set out in paragraph

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[77] See, for example, https://blockbar.com/faq "Does owning the NFT mean ownership of the physical bottle?" (last visited 17 December 2024).

1.94 and in Question 4 above, we do not think it helpful to think of applicable law rules as applying "to" particular types of objects, such as a rare bottle of whisky. To the extent that the question is shorthand for "the law governing property rights to the linked asset", most systems of private international law refer the question of property entitlements to rare bottles of whisky to the *lex situs*, that is, the law of the place where the bottle of whisky is located at the relevant time.

1.125 The question of the "law governing the link" is a little more complex.

1.126 To the extent that the question relates to whether the link is "effective" such that control over the crypto-token in a wallet represents a property right to the underlying asset itself, we do not think it helpful to think in terms of the law applicable "to the link".

1.127 Rather, on a proper characterisation, the issue is ultimately one of property entitlements in relation to the underlying asset. As we set out above, such issues are referred to the *lex situs*. From this, it will be for the law of the place where the bottle of whisky is located at the relevant time to determine whether property rights in bottles of whisky can pass by transfer of an NFT.[78] In this scenario, the apparent private international law question of "what law governs the link" is a substantive property law issue in disguise.[79] This is, however, only made apparent following an exercise in characterisation.

1.128 By contrast, questions relating to the effectiveness of the "link" framed as a claim for breach of the issuer's warranty or obligation that the "link" is indeed effective would more straightforwardly be characterised as a contractual issue.

1.129 The question of the law "governing the token" – or, more appropriately, property rights in the token – is again more complex. Whist the token "is" indeed a digital asset, the extent to which the token itself is an object worth litigating over as an object of property rights depends on the circumstances of each case. Of particular relevance might be the terms on which the issuer has undertaken to exchange the token for underlying asset. For example, simple presentation without more might be sufficient. Alternatively, it may be that the issuer will indeed require more, such as proof of identity.

1.130 In any event, we think that in many cases, it will be unlikely that the token itself will form the object of litigation as an object of property rights. We think our reasoning is more clearly demonstrable by a more everyday example.

1.131 Consider a coat deposited in the cloakroom of a theatre. Upon deposit, a ticket bearing a unique identifier that "links" it to the coat is issued to the depositor by the cloakroom. Upon subsequent presentation of the ticket at the cloakroom, the depositor can redeem their coat.

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78 Many systems require at least delivery of the property object before rights can pass. See further para 12.24 of our Digital assets and ETDs in private international law: which court, which law? (2024) Law Commission Call for Evidence.

79 We took the same position in relation to the question of what law "governs electronic validity" in our ETDs in private international law: FAQs (2024) Law Commission Paper.

1.132 Conceptually, there is little to distinguish this transaction from a bill of lading to bearer; or, indeed, the receipts issued by the seventeenth century goldsmiths in relation to deposits of gold (from which the modern promissory note and banknote developed). The only real commercial difference is that the cloakroom ticket is not intended to be traded, for example, amongst the audience at the theatre.

1.133 If, however, during the course of the performance, the ticket is stolen or lost, the depositor has initially two main options, which each lead to further possibilities:

(1) The depositor may seek to find and recover the ticket from whoever happens to have it; or

(2) The depositor may go directly to the cloakroom and advise that the ticket has been lost.

(a) If the coat is still there, they may seek to identify themselves to the cloakroom as the owner of the coat and to receive the coat or a new ticket allowing them to reclaim the coat later.[80]

(b) If the coat has already been surrendered to a third party who has presented the original ticket, the depositor has several new options:

(i) They may seek compensation from the theatre for loss of the coat. The success of any such personal claim would depend on the terms on which the theatre took (or disclaimed) responsibility for the coat.

(ii) They may seek to find the person who had dishonestly presented the original ticket and seek compensation for interfering with their rights in the ticket.

(iii) They may seek to find the coat and recover it directly from whoever happens to have it.

1.134 From this, we do not think it likely that establishing entitlement to the ticket itself will be a priority. Ultimately, we think the aim will be directed at the coat itself; whether it is still in the cloakroom or has passed into the hands of a third party. If, for example, the coat and ticket were in the hands of two separate third parties, we think it far more likely that a claim would be made to recover the coat. Only if it were not possible to find the coat might claims proceed against the cloakroom and any other third party who can be identified as a potential defendant.

1.135 We think these principles apply equally to the token aspect of linked assets as well as tokens that are used in the context of negotiable instruments. We were told that, in the context of the systems used to facilitate use of electronic bills of lading, disputes as between participants to the electronic system regarding entitlements to the electronic bill of lading itself are unlikely to arise. Rather, if any such entitlement were in issue between participants, the parties would be far more likely to seek to arrest the cargo

[80] Section 69 of the Bills of Exchange Act 1882 similarly provides for the holder's right to request a duplicate of a lost bill.

and make their claim directly against the carrier itself as the person owing the obligation to deliver the cargo.

1.136 In such cases, the ultimate question might not necessarily be "who is entitled to the bill of lading" but the question of "who is the person entitled to give lawful discharge of the carrier's contractual obligation to deliver the cargo?" Such question, moreover, will remain a live legal issue as a matter of contract, even if all three copies of the bill of lading are destroyed or lost.

1.137 For these reasons, we did not give independent treatment to linked assets in our Call for Evidence. We had taken the view that most issues arising from linked assets probably could be resolved by the existing conflict of laws rules after a careful consideration of characterisation.

1.138 Of course, each case must be considered on its own terms. Any token with a "link" to a "real world" underlying asset that is likely to give rise to property disputes as a property object in itself would call for a different analysis. This analysis, however, would have far more in common with our work on other crypto-tokens that are valued as objects of property rights in themselves, such as bitcoin held directly or an art NFT; rather than other "linked assets" where the token itself is of negligible value. In the former analysis, the next questions might proceed along similar lines as those posed by a distributed ledger: whether the token has been issued within a permissioned or permissionless system, with very little turning on the particular commercial context in which the token is being used.

1.139 It is for this reason that we took the decision not to structure our project by reference to specific use cases but rather by reference to the issues that such use cases pose for private international law. This example of linked assets again illustrates why structuring our project by reference to particular use cases might result in a fragmented discussion of the underlying issues insofar as they are relevant and problematic for private international law.

## FOLLOW UP QUESTIONS

1.140 We welcome follow up questions arising from this document, which can be sent to conflictoflaws@lawcommission.gov.uk.