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Digital assets and the (official) dawn of the third category of personal property

The Property (Digital Assets etc) Bill (the **Bill**), introduced on 11 September 2024, addresses a long-standing lack of certainty regarding the legal treatment of 'digital assets' under the laws of England and Wales, and once and for all upends the traditional binary approach to personal property.

The past few years have seen an exponential growth in 'digital assets'. These range from cryptocurrencies like Bitcoin to non-fungible tokens (NFTs) and carbon credits, although given the flexibility of the term, a humble pdf file or email could also be categorised as a digital asset.

The commercial uptake in many forms of digital assets as new commodity classes has had to contend with laws of property developed over hundreds of years in the context of tangible physical goods, leaving the legal status of intangible digital assets in a grey area which the Bill seeks to address.

Personal property and digital assets

The laws of personal property distinguish between two forms of property over which property rights may be exercised:

1. **things (or 'choses') in possession**, which could be anything from a gold bar to yacht, the key characteristic being that they are all tangible and capable of physical possession, allowing the possessor to transfer the asset to a third party by way of physical delivery. If a third party interferes with such an asset, legally, the owner

can take steps to recover physical possession of the asset; and

2. **things in action**, like a debt or share, are intangible assets which represent enforceable contractual rights. As such they cannot be transferred by physical delivery and require some other form of legal action to be transferred from one party to another, like an assignment. If a third party interferes with such an asset, legally, the owner can take steps to enforce the legal rights embodied by the asset.

Many forms of digital assets do not fit neatly into either category. The courts have considered the legal status of certain types of digital assets and have been reluctant to include them within the scope of things in possession because they are virtual, and only tangible things are capable of being possessed but equally digital assets have not been viewed as things in action because, while they are intangible, they do not embody rights capable of being enforced by action (such as contractual rights)¹.

Analysis of the Bill

The potential existence of a third category of property has been considered and acknowledged by the courts but not outright endorsed in the absence of the backing of legislation, which is where the Bill comes into play.

The Bill, which applies to England and Wales, is extremely succinct, with one substantive provision stating that:

"A thing (including a thing that is digital or electronic in nature) is not prevented from being the object of personal property rights merely because it is neither—

(a) a thing in possession, nor

(b) a thing in action."

¹ *AA v Persons unknown* [2020] 4 WLR 35 concerned Bitcoin.

A few points are worth highlighting:

1. **No definition of digital assets** – The Bill simply refers to things *"including a thing that is digital or electronic in nature"* without further elaboration. Initially in the consultation process, the Law Commission had proposed defining *"data objects"* as the third category of personal property, however, this was dropped in light of criticism from consultees that it risked being too restrictive². The drafting of the Bill indicates the government's preference to keep the scope of the legislation as broad and flexible as possible in light of the constantly evolving landscape of digital assets.
2. **No assumption that all forms of digital assets are property** – In line with the lack of a definition, the Bill is not saying that all forms of digital assets are capable of attracting property rights. On this basis, the starting point is to consider whether the thing in question is functionally analogous to things which attract property rights and, if so, if it is capable of attracting such rights despite not clearly falling into either category of thing in possession or a thing in action³. For example, the Law Commission acknowledged that it views *"crypto-tokens"* (which includes cryptocurrencies like Bitcoin) as falling within the third category of personal property, while other categories like voluntary carbon credits are *"potentially"* within scope⁴.
3. **Existing common law principles still apply** – As the Bill does not set out a test for determining what this third category of personal property is, the principles established by common law remain relevant. For example, in *National Provincial Bank v Ainsworth [1965] AC 1175*, Lord Wilberforce summarised the criteria to apply when assessing whether a right or interest constitutes personal property to which rights attach – if it is: (a) definable, (b) identifiable by third parties, (c) capable of assumption by / transfer to third parties, and (d) has a degree of permanence or stability. Over the years, other factors have been considered relevant, such as whether the thing in question is 'rivalrous'⁵, all of which a court can consider on a case-by-case basis.

Practical Impact of the Bill

The combined brevity and broadness of the Bill is an acknowledgment that the common law remains the appropriate forum for determining whether or not a thing constitutes personal property. It does not provide the courts with a specific formula to apply – cases will continue to rely on the application of the existing body of established common law principles to the specific facts of the case. However, the Bill does remove the legal uncertainty as to whether digital assets are capable of being personal property and dispels the traditional binary approach which the courts have been reluctant to overtly upend. The Bill follows the Electronic Trade Documents Act 2023, and it will further reinforce the reputation of England and Wales as a leading jurisdiction, alongside the likes of Singapore, when it comes to the legal treatment of digital assets.

Fittingly, that the Law Commission described the intention of the Bill as *"unlocking the development of the common law"*⁶ without dictating its future course. The developers and holders of many forms of digital assets already assume that their assets constitute personal property and are protected by property rights, and so the Bill represents the legal system playing catch-up.

Therefore, the Bill is unlikely to cause a significant shift in behaviour and its main benefit can be viewed as legal certainty to back up existing behaviour. Parties that own or hold interests in digital assets gain certainty that, in a variety of scenarios, including insolvency, theft or fraud, these assets could be considered to be property over which their rights can be enforced. For example:

1. **Freezing orders** – A court could include qualifying digital assets within the scope of a proprietary freezing injunction in order to prevent the holder dissipating them while a dispute remains unresolved. Cross-border issues remain regarding the official location of the digital asset in question and the discrepancy between how that jurisdiction treats digital assets versus England and Wales – this is the subject of another ongoing Law Commission consultation process⁷;
2. **Bankruptcy & insolvency** – If categorised as property, digital assets could be included within a party's estate, and so could be realised and sold for the benefit of the creditors;

² The Law Commission, Para 3.63 'Digital Assets: Final report', 27 June 2023

³ The Law Commission, Para 3.32, 'Digital assets as personal property: Supplemental report and draft Bill', 29 July 2024

⁴ IBID, Para 1.14

⁵ Law Commission, Para 4.5 'Digital Assets: Final report', 27 June 2023: *"A thing is rivalrous if the use or consumption of the thing*

by one person, or a specific group of persons, necessarily prejudices the use or consumption of that thing by one or more other persons."

⁶ The Law Commission, Para 3.29, 'Digital assets as personal property: Supplemental report and draft Bill', 29 July 2024

⁷ The Law Commission, 'Call for evidence: Digital assets and ETDs in private international law: which court, which law? February 2024

3. **Theft & improper use** – If stolen or otherwise interfered with, including in the case of fraud, a party whose affected assets qualify as property has stronger legal remedies available to them; and
4. **Enforcement of security** – Parties can take security over digital assets with greater certainty that they would be able to successfully enforce these security interests and gain access to the digital assets. However, currently under English law possessory security interests like pledges would most likely still not be appropriate without further development of common law principles, for example potentially adapting to a concept of 'control' rather than possession of digital assets.

The timeframe for implementing the Bill remains to be seen, and it is highly unlikely to represent the final word on the legal treatment of digital assets, as a variety of legal challenges and uncertainties remain, indicating that technology remains a few steps ahead of the law, albeit with one significant pitfall removed.

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