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The New FATF Rules for Crypto Exchanges and Custodians

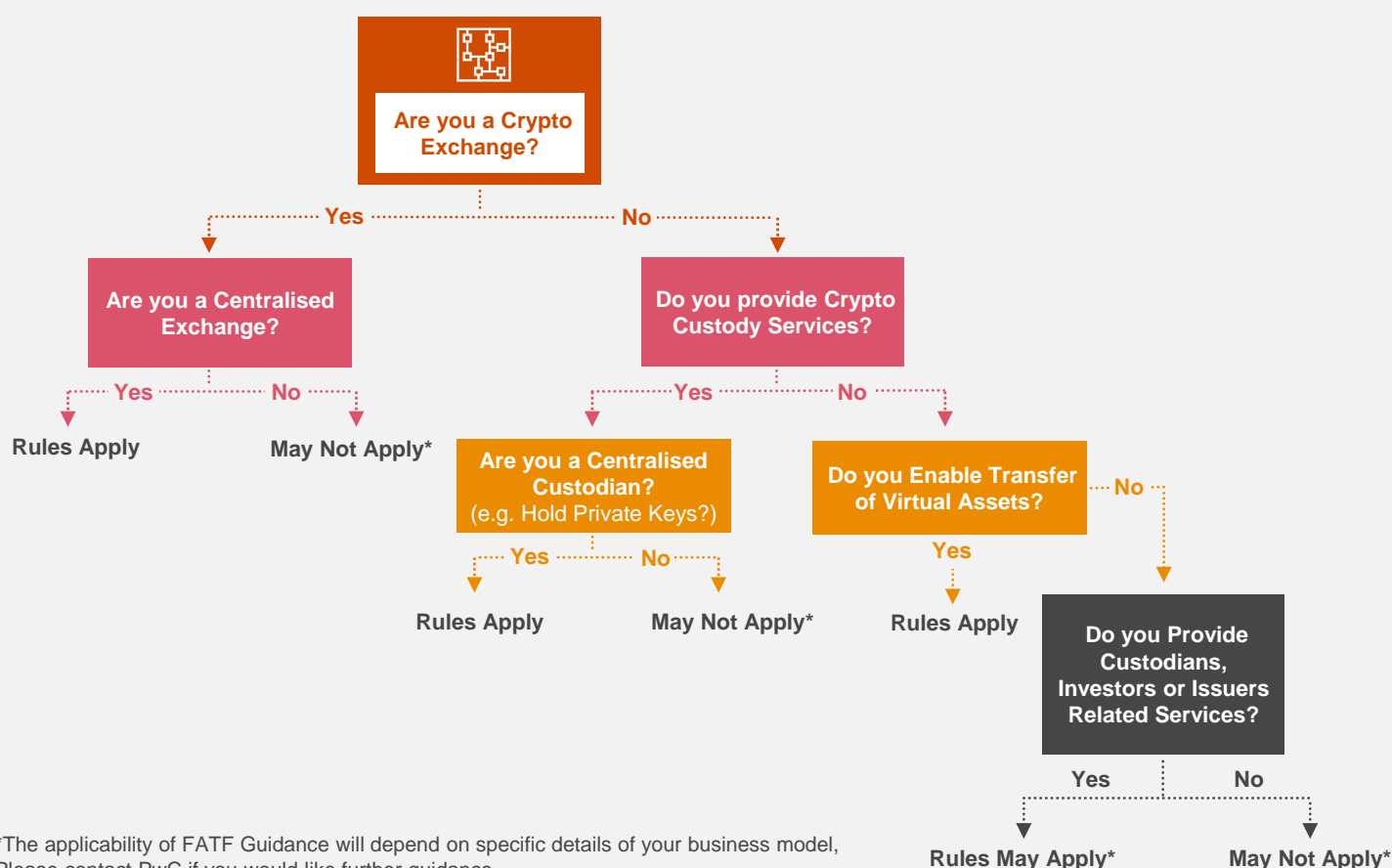
What are the new rules?

In June 2019, the Financial Action Task Force (FATF) adopted an Interpretive Note to Recommendation 15 to further clarify how the FATF requirements should apply in relation to Virtual Assets and Virtual Asset Service Providers.

The Guidance from FATF addresses the application of a risk-based approach (RBA) to Virtual Asset activities or operations and Virtual Asset Service Providers. The guidance covers a range of topics including: supervision or monitoring of Virtual Asset Service Providers for anti-money laundering and terrorist financing (AML/CFT) purposes; licensing or registration; preventive measures, such as customer due diligence, recordkeeping, and suspicious transaction reporting, among others; sanctions and other enforcement measures; and international co-operation.

This updated Guidance expands on the 2015 Virtual Currency Guidance and further explains the application of the risk-based approach to AML/CFT measures for Virtual Assets; identifies the entities that conduct activities or operations relating to Virtual Assets —i.e., Virtual Asset Service Providers; and clarifies the application of the FATF Recommendations to Virtual Assets and Virtual Asset Service Providers.

Do The FATF Rules Apply To You?



To whom do they apply?

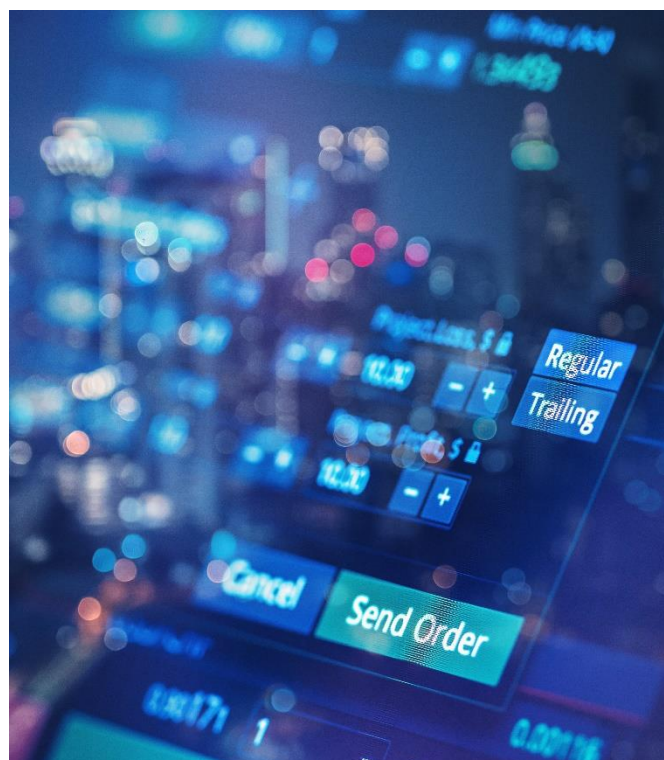
FATF Recommendations require all member jurisdictions to impose specified AML/CFT requirements on Virtual Asset Service Providers as well as traditional financial institutions and designated non-financial businesses and professions such as lawyers and accountants. Through membership in FATF or FATF-style regional bodies, more than 200 countries and territories are affected by the guidance.

FATF has defined a virtual asset and a virtual asset service provider in the following ways:

- “Virtual asset” as a digital representation of value that can be digitally traded or transferred and can be used for payment or investment purposes. Virtual assets do not include digital representations of fiat currencies, securities, and other financial assets that are already covered elsewhere in the FATF Recommendations; and
- “Virtual asset service provider” as any natural or legal person who is not covered elsewhere under the Recommendations and as a business conducts one or more of the following activities or operations for or on behalf of another natural or legal person:
 - Exchange between virtual assets and fiat currencies; (e.g. Fiat-to-Crypto Exchanges)
 - Exchange between one or more forms of virtual assets; (e.g. Crypto-to-Crypto Exchanges)
 - Transfer of virtual assets; and Safekeeping and/or administration of virtual assets or instruments enabling control over virtual assets; (e.g. Crypto Custodians)
 - Participation in and provision of financial services related to an issuer’s offer and/or sale of a virtual asset.

Notably, the scope of the FATF definition includes both Crypto-to-Crypto and Fiat-to-Crypto transactions or financial activities or operations.

Depending on their particular financial activities, Virtual Asset Service Providers include Virtual Asset exchanges and transfer services; some Virtual Asset wallet providers, such as those that host wallets or maintain custody or control over another natural or legal person’s Virtual Assets, wallet(s), and/or private key(s); providers of financial services relating to the issuance, offer, or sale of a Virtual Asset (such as in an ICO); and other possible business models.



When do they need to be implemented?

FATF will conduct a 12-month review in

June 2020

The FATF guidance is designed to be implemented by local regulatory authorities and FATF has explicitly stated that self-regulation will not be acceptable.

The FATF will monitor implementation of the new requirements by jurisdictions and service providers, and will conduct a 12-month review in June 2020. Jurisdictions are expected to have made reasonable and rapid progress towards compliance by this time; however, the exact timing of when regulations come into force will vary from jurisdiction to jurisdiction.

What do you need to do?

Local regulations are required to include all applicable FATF Recommendations. This includes obligations on governments and regulators, as well as market participants. Virtual Asset Service Providers will be required to develop end-to-end AML/CFT control frameworks, which include amongst others:

FATF Recommendation 10

- Virtual Asset Service Providers should design Customer Due Diligence (CDD) processes to help them in assessing the AML/CFT risks associated with covered Virtual Asset activities and customers.
- CDD must be performed in the context of establishing a business relationship or while carrying out occasional transactions for non-customers with a value greater than USD 1,000 or EUR 1,000.
- CDD comprises identifying the customer and applying a risk-based approach to verifying the customer's identity using reliable and independent information, data or documentation. Where the customer is not a natural person, the customer's beneficial ownership must be determined. The CDD process also includes understanding the purpose and intended nature of the business relationship, where relevant, and obtaining further information in higher risk situations.
- Ongoing due diligence of the customer relationship must be performed and transactions must be scrutinised.

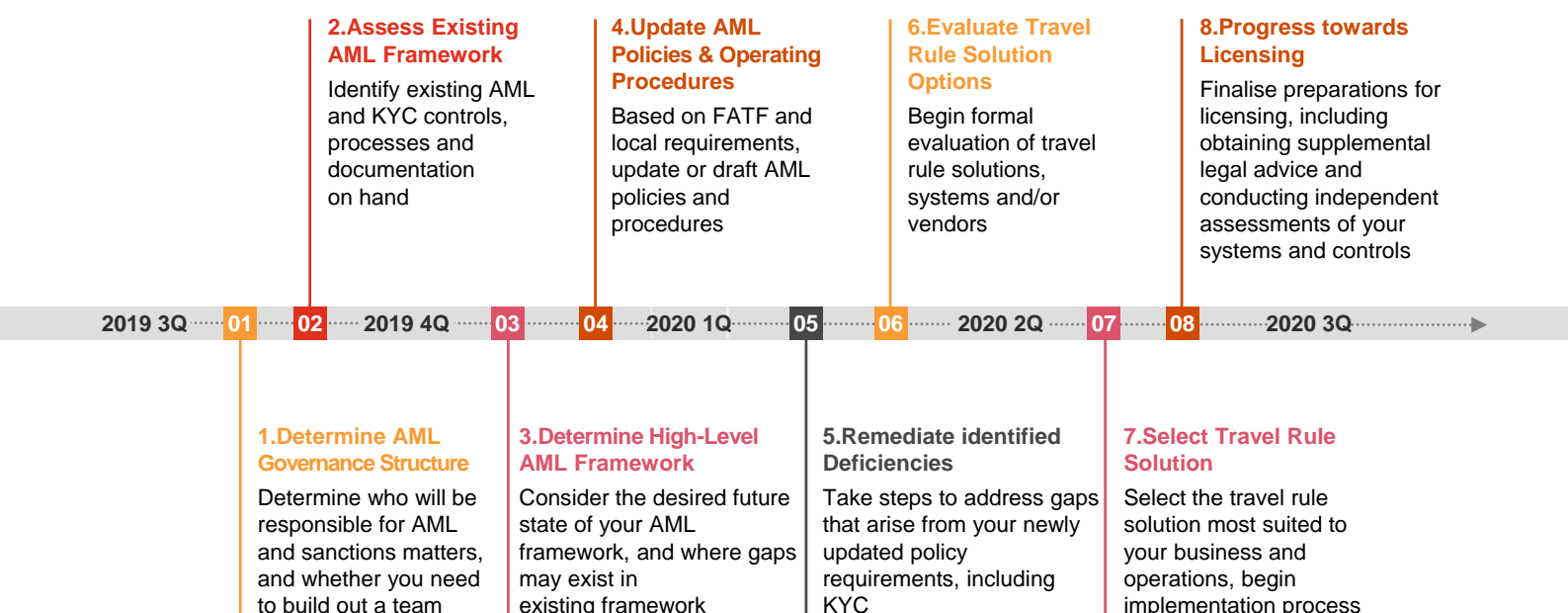
FATF Recommendation 16

- When a Virtual Asset Service Provider conducts a transfer of Virtual Assets on behalf of a customer, it is required to:
 1. Obtain and hold accurate (i.e. verified for accuracy) originator information, including customer name and wallet address, as well as other data such as physical address, date of birth or other specified alternatives;
 2. Obtain and hold beneficiary information, specifically the customer name and wallet address; and
 3. Transmit the originator and beneficiary information to a receiving Virtual Asset Service Provider (or other obliged entity, such as a financial institution), if any. This requirement, which banks already adhere to, is known as the Travel Rule.
- Originator and beneficiary information must be screened to ensure that transactions with designated persons and entities (e.g. those subject to financial sanctions) are identified, reported to competent authorities and subject to freezing measures.

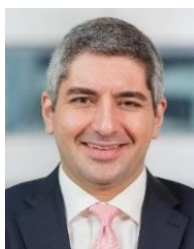


What does this mean for your business?

If you are a Virtual Asset Service Provider you need to start exploring how you will comply with such requirements. However certain elements of the FATF requirements present challenges given today's Virtual Asset infrastructure, especially the Travel Rule. New solutions are required and these may take time.



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