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ARTICLE

Amendments to UK Anti-Money Laundering Legislation – How They Apply to Cryptoasset Businesses

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Background

In April 2018, the EU's Fifth Anti-Money Laundering Directive (the "Directive") was adopted, with a deadline for transposition into national law of 10 January 2020. Although the UK Government consulted on transposition of the Directive in the first half of 2019, other political matters then assumed greater prominence and it was only on 20 December 2019 that the Money Laundering and Terrorist Financing (Amendment) Regulations 2019 (the "2019 Regulations") were laid in Parliament. The 2019 Regulations largely come into force on 10 January 2020 in line with the deadline for transposition.

The 2019 Regulations amend the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the "Money Laundering Regulations"), which transposed into national law the Fourth Anti-Money Laundering Directive. Minor amendments are also made by the 2019 Regulations to the Terrorism Act 2000, the Proceeds of Crime Act 2002, the Companies Act 2006 and other companies legislation in order to align definitions and in order to implement requirements relating to companies.

This article considers the amendments to the UK anti-money laundering regime made by the 2019 Regulations insofar as they relate specifically to cryptoasset businesses.

Who do the 2019 Regulations apply to?

Under the 2019 Regulations, cryptoasset exchange providers and custodian wallet providers are now "relevant persons" (equivalent to "obliged entities" within the Directive) who will now be subject to the requirements of the Money Laundering Regulations, which include obligations relating to customer due diligence and reporting of suspicious transactions. In the 2019 Regulations, the Government has chosen to take a broader approach than that of the Directive, in respect of exchange providers in particular. The Directive applies to "providers engaged in exchange services between virtual currencies and fiat currencies" where "virtual currencies" means:

> *"A digital representation of value that is not issued or guaranteed by a central bank or a public authority, is not necessarily attached to a legally established currency and does not possess a legal status of currency or money, but is accepted by natural or legal persons as a means of exchange and which can be transferred, stored and traded electronically".*

Whereas, the 2019 Regulations apply to "cryptoasset exchange providers" where "cryptoasset" means:

> *"A cryptographically secured digital representation of value or contractual rights that uses a form of distributed ledger technology and can be transferred, stored or traded electronically".*

This is an adoption of the definition of cryptoassets from the Final Report of the UK's Cryptoassets Taskforce[1]. Unlike the Directive definition of virtual currencies, it requires the use of distributed ledger technology. HM Treasury believes that the chosen definition is "more specific and precise" but still meets the EU's ultimate intention. The chosen definition is also wide enough to capture exchange, security and utility tokens.

In addition, the definition of cryptoasset exchange provider[2] includes (by way of deviation from the minimum requirements set out in the Directive) where the firm or sole practitioner in question:

- Offers exchange services "as creator or issuer of any of the cryptoassets involved," therefore it explicitly applies to initial coin offerings ("ICOs"). The UK Government views ICOs as another point of exchange at which those in possession of illicit funds could launder their money into a new, clean cryptoasset, obfuscating the original source or purpose of such funds; or
- Offers exchange services of one cryptoasset for another. The Directive definition refers only to "providers engaged in exchange services between virtual currencies and fiat currencies"; or
- Operates a machine which utilises automated processes to exchange cryptoassets for money or money for cryptoassets.

What else is new in the 2019 Regulations?

Regulation 56 of the Money Laundering Regulations contains a requirement to be registered, which now, by virtue of the 2019 Regulations, extends to a person who wants to act as a cryptoasset exchange provider or custodian wallet

provider. The Financial Conduct Authority (FCA) is under a duty to maintain the register of cryptoasset exchange providers and custodian wallet providers. The 2019 Regulations provide for a transitional period in respect of cryptoasset exchange providers and custodian wallet providers that were carrying on business as such in the UK immediately prior to 10 January 2020, which will last until 10 January 2021.

The 2019 Regulations also include a new provision on the "fit and proper test" for registration as it applies to cryptoasset businesses[3]. This requires that the applicant and any officer, manager or beneficial owner of the applicant, must be a fit and proper person to carry on the business of a cryptoasset exchange provider or custodian wallet provider, as the case may be. A person who has been convicted of certain criminal offences (including, *inter alia*, perjury, counterfeiting, money laundering and terrorism-related offences) is to be treated as not being fit and proper. Absent conviction for a specified criminal offence, the 2019 Regulations set out those factors to which the FCA must have regard in its consideration of the test.

In addition, where a cryptoasset exchange provider or custodian wallet provider establishes a business relationship or enters into a transaction as part of its activities for which it is registered, and where the activity is not subject to the protections of the Financial Ombudsman Service and/or the Financial Services Compensation Scheme, they must inform the customer in advance that the activity is not subject to such protections.

The 2019 Regulations also confer new powers on the FCA in respect of directions that the FCA may make in its role as supervisory body.

Conclusion

The Government's decision to include additional regulatory provisions when transposing the Directive was trailed in its consultation document[4]. Although responses to the consultation have yet to be published, it is understood that there was "significant engagement" from respondents on the scope of the anti-money laundering regime for cryptoasset businesses. The Government has taken account of these responses and the amendments in the 2019 Regulations have not gone as far as perhaps they could have gone after respondents unanimously agreed that publishers of open-source software (and, by extension, non-custodian wallet providers) should not be brought within the scope of the new regime.

The amendments made by the 2019 Regulations to the anti-money laundering regime represent a significant step up in terms of the regulation and oversight of cryptoasset businesses, albeit it is perhaps only the first step towards a more comprehensive regime targeted specifically at cryptoassets.

[1]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/752070/cryptoassets_taskforce_final_report_fin

[2] Regulation 14A(1) of the 2019 Regulations

[3] Regulation 58A

[4]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/795670/20190415_Consultation_on_the_Transp

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