



## **FCA Cryptoasset registrations**

### **Guide 3: FCA feedback on applications (Part 1)**

Guidance is provided for firms and is not intended as legal advice.

#### **Background**

The FCA are the anti-money laundering (“AML”) and counter-terrorist financing (“CTF”) supervisor of UK cryptoasset businesses under the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (“MLR”). Firms proposing to conduct cryptoasset activities in the UK must register with the FCA beforehand. Cryptoasset firms are often referred to as Virtual Asset Service Providers (“VASP”).

Individuals and businesses have to register with the FCA for AML and CTF purposes, if they are carrying on cryptoasset activities that are:

- (i) within scope of the MLR
- (ii) if this activity is in the course of business; and
- (iii) if the activity is carried on in the United Kingdom.

The FCA recommend that legal advice is sought regarding whether your business requires registration before engaging in the application process.

A cryptoasset registration is different from authorisation as an Electronic Money Institution (“EMI”) or Payment Institution (“PI”). An EMI or PI wishing to undertake cryptoasset activities in the UK will still need to register with the FCA as a separate application process.

In January 2023, the FCA published feedback on “*good and poor quality applications*” – their findings are the subject of this first guide. A second guide will further explore this helpful feedback.

#### **FCA feedback on “good and poor quality applications”**

In January 2023 the FCA published initial feedback discussing what elements they deem to be associated with “good quality” and “poor quality” applications that have been made in accordance with the requirement to register cryptoasset firms under the MLR. Most recently, at the time of writing, further feedback was provided in September 2023.

The FCA intend that the feedback helps improve the quality of future applications in order to help make the process as simple and efficient as possible. All firms intending to submit an



application for registration would be well advised to review the FCA's feedback in addition to the guidance published on their website.

The FCA provided their feedback in a number of distinct areas, which are addressed in a two part set of guides. This first guide addresses feedback on the background to preparing an application, specifically what information should be reviewed, whether the activity constitutes cryptoasset activities and if the activity requires UK registration. We also address the important issue of appointing an MLRO. The second guide looks at some of the detail of an application where the FCA have identified issues, including the service description, business plan, risk assessment arrangements, systems, policies and procedures.

## **1. Review the MLRs**

The FCA "*expect applicants to demonstrate an understanding of the UK AML registration regime as set out in the MLRs*".

This should not be difficult for applicants to address since firms intending to operate in the Fintech market (who may already be authorised in some form) should have a good understanding of the requirements of the MLR. If not, then management should seriously consider the wisdom of providing financial / crypto services given that the directors will be ultimately responsible for compliance with the MLR (and are on the 'hook' in the event of a failure – think fines, public censure, jail time).

Applicants should be clear on how the AML / CTF requirements impact their proposed services, for description in the application, including in the following areas:

- Risk assessment
- Customer due diligence
- Transaction monitoring
- Sanctions screening
- Politically Exposed Persons
- Reporting of suspicious activity; and
- Responsibility for AML / CTF operations.

As part of the preparation of an application for registration it would be wise to prepare an AML Manual. Whilst not necessarily submitted to the FCA (unless requested), the process of preparing the AML Manual will assist the preparation of the descriptions of the AML / CTF policies and procedures that will need to be provided in the application. If the AML Manual is to be submitted as part of the application, care should be taken to ensure that it addresses the information required by the FCA, see ***Cryptoasset registration: Guide 1 - Overview of requirements***.

## **2. Establish whether the cryptoasset activity is within the scope of the MLR**

What are the intended cryptoasset services?

The FCA suggest that applicants refer to their flowchart (see Appendix 1 of this document) and consider if they will be carrying on relevant cryptoasset activities by way of business. The six cryptoasset activities are:

- The exchange of fiat currency for cryptoassets
- Providing custodian wallets for storing cryptoassets on behalf of customers
- The exchange of one cryptoassets for another
- Operating cryptoasset ATMs
- Facilitating the peer-to-peer exchange of cryptoassets; and

- Participation in Initial Coin Offerings.

This is an area where applicants should certainly seek expert advice. As with all regulatory applications it is critical to have a clear understanding on the scope and functionality of the intended services, i.e. a documented and agreed ‘service description’.

The subject of preparing a service description, in the context of EMI / PI businesses, is addressed in this guide - ***Applications for Authorisation: Guide 1 – Permissions***. The process described would be the same for cryptoasset firms. Applicants will also need to consider the development of the services, in the near term, which may need to be covered in the application, see this guide for more background: ***Applications for Authorisation: Guide 2 - Service development***.

A clear understanding of the cryptoasset services to be provided (and their near-term development) is the foundation of any good application.

### Carrying on business in the UK

Firms will also need to consider if they will be carrying on business in the UK. This is not always clear cut but would certainly include maintaining a UK office or actively marketing services to UK customers. The FCA State that *“An applicant that only has a satellite office in the UK and has all of its operations and day to day management outside of the UK may not be carrying on relevant cryptoasset activities by way of business”*. This is another area where applicants should seek expert advice from the outset of an application process.

### **3. Consider seeking independent legal / compliance advice**

The FCA suggest that applicants should consider seeking independent legal or compliance advice as part of preparing an application. The FCA highlight the careful consideration of the *“nature of the products and applicable regulations”*. As stated above, it is essential to the success of an application to have a clear, well understood and articulated service description that aligns with required regulatory permissions (as well as having considered how the proposed services will develop).

### **4. Review the information on the FCA’s website and the registration form**

Information published by the FCA should be reviewed prior to preparing the application. In their feedback, the FCA suggest that applicants should review all of the information on their website, the FCA Register, the Connect system (through which the application is submitted) and the cryptoasset registration form (which is completed in the Connect system). The requirements for an application for registration are summarised in this guide - ***Cryptoasset registration: Guide 1 - Overview of requirements***.

A key part of the submission will be the Regulatory Business Plan (“RBP”); this document will contain the majority of the information that is submitted to the FCA and needs to be carefully prepared. The RBP will supplement the application form and provides an opportunity for the applicant to demonstrate that it is *“ready, willing and organised”* to be registered as a cryptoasset service provider. Further information on the preparation of an RBP, albeit in the context of an application for authorisation as an EMI / PI, is provided here, ***Applications for Authorisation: Guide 11 - Preparing a Regulatory Business Plan***.

### **5. Appoint a Money Laundering Reporting Officer**

Money Laundering Reporting Officer

An applicant firm must appoint a Money Laundering Reporting Officer (“MLRO”) with “*relevant knowledge, experience and training*”. The role of MLRO should have “*a level of authority, independence and sufficient access to resources and information*” in order to perform their role. The requirement to appoint an MLRO with oversight for the AML compliance is defined in the MLR.

The FCA state that they “*will look carefully at MLRO / Nominated Officers who are not based in the UK*”. It would be unusual to have the MLRO located outside the UK and if this were to be proposed in the application, the applicant would need to present some robust reasoning.

### Nominated Officer

Applicants must also appoint an individual as "Nominated Officer" which is defined as the person receiving and submitting SARs under Part 7 of the Proceeds of Crime Act 2002, Part 3 of the Terrorism Act 2000 and Reg. 21(3) MLR 2017. It is common practice for the same individual to perform the MLRO role and act as the firms' Nominated Officer.

### MLRO job description

It would be advisable to prepare a job description, defining the responsibilities of the MLRO role. The job description would be used within the business to guide recruitment of a suitable individual, the performance of initial and ongoing assessments of their fitness and propriety and to guide the provision of relevant training in order to maintain the ‘competence and capability’ of the individual on an ongoing basis.

### MLRO involvement in the application process

The FCA expect that the MLRO will be fully involved in the preparation of the application (not surprising given that the application is for an AML Registration under the MLR). This will necessitate the early recruitment of a suitable individual – waiting until later in the application process, to save costs, may not therefore be advisable. Firms should also consider the lead-times involved in finding suitable compliance staff, especially those with relevant cryptoasset experience (which the FCA require).

### MLR Individual Form

An MLR Individual Form will need to be submitted as part of the registration application in order to provide the FCA with details of the individual that is proposed to perform the MLRO role. The ‘form’ is actually completed in the FCA’s Connect system. Information to be provided in the MLR Individual Form will be used by the FCA to assess the “*fitness and propriety*” of the individual and includes:

- Individual details – personal details on the individual
- Individual arrangements – details of the nature of the arrangement between the individual and the applicant firm
- Employment history - a full five-year employment history with all gaps explained.
- Fitness and propriety – declarations in relation to criminal and civil proceedings, business and employment matters, regulatory matters; and
- Supplementary information – information relevant to the consideration of fitness and propriety (if relevant).

### The FCA’s fit and proper assessment

The fit and proper assessment will include whether the MLRO has adequate skills and experience to perform the role, including whether the individual has a sufficient understanding

of “cryptoasset-related technologies and the ability to manage the specific risks arising from dealing with cryptoassets, their custody, exchange as well as initial coin offerings”. The shortage of suitably experienced / qualified MLRO's is understood by the FCA but will not affect their assessment. The requirement to have specific cryptoasset experience exacerbates this shortage. The FCA would typically view a competent MLRO from the financial industry who has general experience plus either some crypto specific experience or crypto-risk training<sup>1</sup> as being appropriate for meeting the fit and proper requirement.

A key area for refusal of applications for registration by the FCA is where the MLRO lacks fitness and propriety. A lot therefore depends on finding a good quality and motivated MLRO – we can help with the recruitment process.

#### Due diligence on recruitment

It is common for businesses to perform due diligence on potential new staff as part of a recruitment process, particularly during the final stages of recruitment and before an offer of employment is made.

A staff due diligence process within a cryptoasset firm should involve some additional checks designed to ensure that candidates for the MLRO role are able to meet the FCA’s fitness and propriety requirements and have the necessary cryptoasset experience. The checks required to ensure the FCA’s fitness and propriety requirements are met could be incorporated into the standard staff due diligence process. Further guidance on the due diligence process, in the context of payments firms, is available here: ***Compliance Arrangements: Guide 6 - EMD PSD Individuals***.

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<sup>1</sup> There is no standard crypto-related qualification, although Elliptic, ACAMS and BPP offer courses with relevant qualifications.

## Appendix I – FCA Flowchart: Do I need to register with the FCA for carrying on cryptoasset activity?

