

WFE Response to the Financial Action Task Force – Mitigating Risks from Virtual Assets



Background

We are grateful for the opportunity to respond to the Financial Action Task Force's Recommendations as they relate to mitigating risks associated from virtual assets and virtual asset services providers (VASPs), specifically in relation to Paragraph 7(b) of the Interpretative Note.

The World Federation of Exchanges (WFE) is the global trade association for regulated exchanges and clearing houses. We represent over 250 market-infrastructure providers, spread across the Asia-Pacific region (~37%), EMEA (~43%) and the Americas (~21%). Some of our members are highly invested in the crypto space through the offerings of coin-backed ETFs or the operation of their own cryptoasset platforms.

With extensive experience of developing and enforcing high standards of conduct, WFE members support an orderly, secure, fair and transparent environment for all sorts of investors and companies wishing to raise capital and manage financial risk.

We seek outcomes that maximise financial stability, consumer confidence and economic growth. We also engage with policy makers and regulators in an open, collaborative way, reflecting the central, public role that exchanges and CCPs play in an internationally integrated financial system.

Introduction

Cryptoassets are becoming increasingly important in all sectors of the capital market space. Their use in capital-raising processes, peer-to-peer lending, investment strategies and as a medium of exchange have grown gradually. Globally, regulators are becoming more proactive in dealing with cryptoassets by reviewing existing regulation, creating new frameworks, building task forces and enhancing investor education.

The FATF's recommendations are timely and the WFE welcomes the recommendations and supports the approach taken by FATF to mitigating the risks posed by virtual asset service providers. Identifying those making and receiving payments is fundamental to that. Whilst the cryptoasset market is maturing, there are several reasons why the cryptoasset space should be placed under closer inspection. Mainly, there is a need for tighter oversight of cryptoasset-platforms from the viewpoint of investor protection and market integrity. Risks such as the threat of hack attacks and 'bubbles' that could have implications for financial stability also lend impetus to the call for stricter regulation. Accordingly, the WFE believes that any regional debate should inform international debates to ensure regulatory coherence across jurisdictions.

The WFE believes that a danger, often overlooked, lies in calling the VASPs, of which many are cryptoasset platforms, "exchanges" which might lead investors into thinking that all such platforms are regulated or that all meet the regulatory standards of the world's leading securities and derivatives exchanges.

The WFE welcomes this consultation and the associated work of the FATF to develop formalised recommendations and guidance to mitigate for money laundering/terrorist financing risks associated with cryptoasset platforms.

If you have any further questions, or wish to follow-up on our contribution, the WFE remains at your disposal. Please contact:

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Questions

The FATF invites private sector entities and other experts to provide written comments on paragraph 7(b).

7 (b) Countries should ensure that originating VASPs obtain and hold required and accurate originator information and required beneficiary information on virtual asset transfers, submit the above information to beneficiary VASPs and counterparts (if any), and make it available on request to appropriate authorities. It is not necessary for this information to be attached directly to virtual asset transfers. Countries should ensure that beneficiary VASPs obtain and hold required originator information and required and accurate beneficiary information on virtual asset transfers, and make it available on request to appropriate authorities. Other requirements of R.16 (including monitoring of the availability of information, and taking freezing action and prohibiting transactions with designated persons and entities) apply on the same basis as set out in R.16

We welcome the opportunity to provide comments on the FATF's public statement on mitigating risks associated from virtual assets and virtual asset services providers (VASPs), specifically in relation to Paragraph 7(b) of the Interpretative Note.

Whilst new technologies can bring significant benefits to the industry, we must also be conscious that risks must be carefully managed.

Markets are global, and as such it is only right that guidelines are designed at the global level to reflect this. The WFE welcomes well-designed international efforts to enhance and strengthen the principles of regulation and supervision to safeguard users and mitigate for risks which include money laundering/terrorist financing (ML/TF). WFE, therefore, supports the recommendations and actions proposed by FATF in mitigating the ML/TF risks with virtual asset service providers.

The WFE and its members share CPMI-IOSCO's goals of ensuring the safety and soundness of the global financial system, exemplified through initiatives such as the Principles for Financial Market Infrastructure (PFMI)¹, which are critical to enhancing investor and consumer confidence, and promoting economic growth. Adherence to these values are integral to the Market Infrastructure's ability to support market integrity both now and in the future².

As part of that application of PFMI, regulations such as AML/CFT are endemic within regulated market infrastructures such as exchanges and CCPs. As regulated market infrastructures, they are bound by international, regional and domestic standards in order to carry out their financial activities. VASPs, in the form of crypto-platforms, as they currently operate, that purport to act as 'exchanges' are not necessarily governed by such monitoring and supervisory provisions (or required to be).

To that end, WFE would like to highlight the importance of distinguishing between what are so-called "cryptoasset exchanges" and the regulated, secure and lit markets that real exchanges provide. Since the emergence and popularity of cryptocurrencies (Bitcoin, Ethereum, and many more), cryptoasset platforms have been referred to as "exchanges", which can lull investors into thinking that they are all regulated or that all meet the regulatory standards of established national exchanges.

¹ CPMI-IOSCO's Principles for Financial Market Infrastructures (PFMI), April 2012, https://www.bis.org/cpmi/info_pfmi.htm

² WFE, Oliver Wyman, Market infrastructures and market integrity: A post-crisis journey and a vision for the future, April 2018, <https://www.world-exchanges.org/our-work/articles/wfe-oliver-wyman-market-integrity-report>

While some cryptoasset platforms enforce their own standards or must apply some regulation, dependent on the jurisdiction, not all are recognised by regulatory authorities and hence do not necessarily offer the same security to market participants.

With consumer protection and market integrity in mind, cryptoasset platforms and their users would benefit from greater clarity when navigating regulatory obligations e.g. registration, licensing, and investor disclosure – incorporating the type of requirements recommended by FATF.

We believe that a clear distinction should be made between these two service providers, through a form of regulatory recognition, in order to avoid confusion for investors and potentially present them with a sense of false security.

Additionally, if crypto-platforms are going to continue to be referred to as “exchanges”, we urge regulatory authorities to ensure that the platforms demonstrate to participants and users that they meet the appropriate standards. Identifying those making and receiving payments is fundamental to that.

However, it is not only the traditional exchanges that adhere to these regulations but also the related eco-system. Most notably, brokers and investment managers face requirements over client-asset protection, alongside accounting and auditing disciplines – all intertwined with domestic and international standards as part of an integrated system. This combination of related service providers adhering to regulatory requirements in order to serve an exchange further strengthens the protections against ML/TF by virtue of operating through and alongside other regulated entities. In the mainstream, cryptoasset platforms do not have such regulated service providers facilitating transactions.

It is also important that the application of pre-emptive measures, as part of FATF’s AML/CFT recommendations, are ensured to mitigate against the decentralised nature of some VASPs. WFE would encourage the application of regulations, such as KYC, at an early stage in transactions by VASPs to provide greater certainty over the ability to effect the freezing or confiscation of assets should sanctions need to be imposed.