



CUMMINGS PEPPERDINE ON CRYPTO AND THE TRAVEL RULE

WHAT IS THE TRAVEL RULE?

The Travel Rule is part of the international anti-money laundering (“AML”) and counter-terrorist financing (“CTF”) standards put in place by the Financial Action Task Force (“FATF”). It is intended to guard against money laundering and other illegal actions and now applies to the world of crypto as well as more traditional forms of finance.

While crypto was not originally included by FATF, in June 2019, they updated Recommendation 16 to bring crypto within its scope, based on their view that this was needed to be able to mitigate the money laundering and terrorist financing risks associated with virtual asset activities. It covers what European Union terminology calls Virtual Asset Service Providers (“VASPs”) and includes exchanges, banks, over-the-counter desks, hosted wallets and other financial institutions, to share certain identifying information about the recipient and receiver of cryptocurrency transactions over USD/EUR 1000 globally.

The issue now is for the right packages to be found to help provide an IT solution. This is something which is available in the more traditional finance world, such as hedge funds which need to navigate the Travel Rule and data protection rules. The good news is that solutions are available.

These solutions will also need to deal with the characteristics of crypto which would, at first glance, seem to contradict the openness and transparency required by the Travel Rule, for example anonymity and decentralisation.

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The Travel Rule is found in Recommendation 16 of FATF's "International Standards on Combating Money Laundering and the Financing of Terrorist & Proliferation" (the "2012 Standards") and can be found online at:
[\(http://www.fatf-gafi.org/\)](http://www.fatf-gafi.org/)

THE FCA AND THE TRAVEL RULE

The FCA is involved in the Travel Rule, with its latest publication being a consultation in June 2022, so recently (the "FCA CP"). It can be found online at :
<https://assets.publishing.service.gov.uk>

While the FCA CP makes it clear that rules are almost certainly coming, FCA CP does offer hope to the world of crypto. It is clear that the FCA has listened to feedback and is considering adaptations which will be more attuned to crypto, albeit that regulation is coming.

To give three examples which indicate a nuanced approach:

1. the government has agreed that the new legislation will, when put in place, make it clear that the Travel Rule will only apply to those intermediaries that are cryptoasset exchange providers or custodian wallet providers. Importantly, it will not capture other intermediaries, such as software providers;
2. the FCA states that it is in favour of a grace period, and taking into account the current status of compliance technology, the government has decided to allow a 12-month grace period, to run from the point at which the amendments to the MLRs take effect until 1 September 2023. During this period, cryptoasset businesses will be expected to implement solutions to enable compliance with the Travel Rule; and
3. the FCA notes the FATF position that unverified information collected regarding un-hosted wallet transfers is verified, and that to require that the collected information to be verified would present practical difficulties for both the users of cryptoassets and cryptoasset businesses and would not, in

many cases, be practical. As a result, the UK has decided against amending the proposals to require verification.

WHO IS FATF AND WHAT DOES IT DO?

FATF is an independent inter-governmental policy making body which describes itself as a task force composed of member governments. It was established in 1989 by the G7 to examine money laundering trends and techniques, and develop measures to combat money laundering. In 2001, the FATF expanded its mandate to focus on combating terrorist financing in addition to money laundering.

FATF's objectives are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system.

It has 39 members, all listed below.

WHAT ARE THE FATF STANDARDS?

FATF has developed a series of standards, which are recognised as the international standards for combating money laundering, the financing of terrorism and the proliferation of weapons of mass destruction. In this note we look at the 2012 Standards and The Travel Rule, which is found at Recommendation 16.

GUIDANCE AND BEST PRACTICE

As well as producing its standards, FATF also publishes guidance, materials on best practice and other papers that are designed to assist with interpretation of, and compliance with, the standards. These materials are available on the FATF website.

WHAT DO THE 2012 STANDARDS COVER?

The 2012 standards cover the following areas:

1. AML and CTF policies and co-ordination (Section A);
2. Money laundering and confiscation (Section B);
3. Terrorist financing and financing of proliferation (Section C);
4. Preventive measures (Section D);
5. Transparency and beneficial ownership of legal persons and arrangements (Section E);
6. Powers and responsibilities of competent authorities and other institutional measures (Section F); and
7. International co-operation (Section G).

It is in Section D (preventative measures) that we find R.16, the Travel Rule.

RECOMMENDATION 16: THE TRAVEL RULE

The thinking behind the Travel Rule is that by adhering to it, FATF countries will help in the battle to block terrorist financing, stop payments to sanctioned individuals, entities, and countries, enable law enforcement to subpoena transaction details, support the reporting of suspicious activities and prevent the money laundering of cryptoassets.

Recommendation 16 of the 2012 standards require financial institutions to:

1. include required and accurate originator information, as well as required beneficiary information, on wire transfers and related messages;
2. ensure that the information remains with the wire transfer or related message throughout the payment chain;
3. monitor wire transfers for the purpose of detecting those that lack the required

- originator or beneficiary information, or both, and take appropriate measures; and
4. take freezing action and prohibit conducting transactions with designated persons and entities, relating to the prevention and suppression of terrorism and terrorist financing.

However, while these steps impose significant work for traditional financial players, there are specific issues which can cause problems for the crypto arena where anonymity is common. These including working out whether a counterparty VASP is registered under the relevant money laundering regulations and how to deal with cybersecurity, privacy and data protection in a financial arena which is at the vanguard of the use of technology in relation to assets.

Key to meeting the rules is therefore to gather all information, and where dealing with a registered entity this should be possible due to the nature of on-boarding information which such registered entity is required to source for each client.

Where the other party to a transaction is not registered, for whatever reason, this may be more difficult. However, if serious players in the world of digital assets want to avoid misuse of crypto assets, a voluntary adherence to high standards can only set them apart as ahead of the pack.

The issue now is for the right packages to be found to help provide an IT solution. This is something which is available in the more traditional finance world, such as hedge funds which need to navigate the Travel Rule and data protection rules.

INTERPRETATIVE NOTE TO THE TRAVEL RULE

The interpretative note that the aim of this recommendation is to prevent terrorists and other criminals from having unfettered access to wire transfers for moving their funds, and for detecting such misuse when it occurs.

Specifically, the Travel Rule aims to ensure that basic information on the originator and beneficiary of wire transfers is immediately available to law enforcement authorities, prosecution authorities and FIUs.

Where a cross-border transaction is entered into it must have the information set out below, and if this is also adhered to for domestic purposes, a high standard will have been adhere to:

- a. the name of the originator;
- b. the originator account number where such an account is used to process the transaction;
- c. the originator's address, or national identity number, or customer identification number, or date and place of birth;
- d. the name of the beneficiary; and
- e. the beneficiary account number where such an account is used to process the transaction.

In the absence of an account, a unique transaction reference number should be included which permits traceability of the transaction.

The interpretative note also covers the following topics:

1. Scope;
2. Cross-border qualifying wire transfers;
3. Domestic wire transfers;
4. Responsibilities of ordering, intermediary and beneficiary financial institutions; and
5. MVTs operators.

FATF MEMBERS

The members of FATF are:

Argentina
Australia
Austria
Belgium
Brazil
Canada
China
Denmark
European Commission
Finland
France
Germany
Greece
Gulf Co-operation Council
Hong Kong, China
Iceland
India
Ireland
Israel
Italy
Japan
Luxembourg
Malaysia
Mexico
New Zealand
Norway
Portugal
Republic of Korea
Russian Federation
Saudi Arabia
Singapore
South Africa
Spain
Sweden
Switzerland
The Netherlands
Turkey
UK
US

(Note: restrictions have been imposed on the Russian Federation's role and influence within the FATF.)

THE TEAM

Cummings Pepperdine is a leading advisor in crypto. We are one of a select few that advises a large and diverse global client base in the crypto space and the only to provide a complete crypto solution building on the three key areas of law, tax and FCA with legal underpinning at every point.

In law, we have a team of qualified and regulated solicitors and barrister who retains right of audience.

In tax, we have one of the only crypto tax advisors who is both a qualified solicitor and qualified chartered accountant.

In regulation, our team comprises specialists in crypto compliance monitoring structures and governance oversight who are known to the FCA for the quality of their work.

The team is led by Claire Cummings, a leading solicitor specialising in crypto law and the current and evolving regulation. Claire is on the advisory boards of a crypto exchange and an NFT gaming guild and is also a member of the Global Digital Finance working group on



Claire Cummings

stablecoins. Claire has also acted as compliance officer, MLRO and director of an FCA regulated fund manager and qualified under SIB to trade derivatives. As a leading expert in crypto, Claire is a sought after speaker and has published multiple articles on the legal and regulatory issues surrounding cryptocurrencies and the crypto eco-system. Claire is named at the Top 10 influencer in London for hedge funds (2&20, 2022) and is included in the CityWealth Crypto Top 100

The Cummings Pepperdine Online Training Programme, includes sections focussing on Crypto and the Travel Rule, has been designed by a specialist board of compliance consultants, solicitors, chartered accountants, tax advisors and regulatory consultants. We believe that we are the only firm which offers training created by this range of qualified advisors.

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