

# Virtual Assets Money Laundering & Terrorist Financing

## National Risk Overview



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## Introductory statement

This report has been produced within the National Financial Crime Structure which Jersey adopted in 2020 and builds on input and feedback from all relevant competent authorities, as well as from sector representatives within industry.

The Government of Jersey is grateful for all their work, which has enabled us as a jurisdiction to gain a better understanding of the risks we are exposed to. Special thanks are extended to the Jersey Financial Services Commission and XReg Consultants who were key to the production of this report, representing another testament to our commitment to combatting financial crime *together*.

This report is published during the period of sensitivity preceding the 22 June 2022 election and therefore does not contain a ministerial foreword.

## Executive summary

- 1 The Financial Action Task Force (**FATF**), in its role as the international standard-setting body to combat money laundering (**ML**), terrorist financing (**TF**), and proliferation financing (**PF**) requires countries to identify, assess, and understand the risks of ML, TF, and PF they face to ensure adequate mitigating measures are established at a national level. To comply with this requirement, countries must undertake a risk assessment to consider the threats and vulnerabilities specific to them, which stem from factors such as their geographical position, their available legislative and regulatory tools, the industry sectors that operate within their borders, the delivery channels used by entities in the jurisdiction, the types of customers that are serviced, and, importantly, the level of knowledge and understanding of ML and TF risks by authorities and industry.
- 2 The Government of Jersey (**GoJ**) published its first assessment of the jurisdiction's exposure to ML and TF risks in its 2020 and 2021 reports. The assessments rated Jersey's overall ML threat as medium-high and its overall risk of being used as a conduit for TF as medium-low. The GoJ employed the World Bank's methodology in undertaking its National Risk Assessments (**NRAs**); however, neither assessment considered the virtual asset sector. As a result, the GoJ has worked with a series of public and private sector stakeholders and experts in the Virtual Asset Service Provider (**VASP**) sector on a high-level risk overview of the jurisdiction's exposure to ML and TF risks stemming from virtual assets and related activities during Q4 2021/Q1 2022.
- 3 Jersey has been progressive in the area of virtual assets and has continued to monitor the threat and risks they pose to the jurisdiction informally since their emergence. This is exemplified by the fact that Jersey brought within scope of AML provisions entities that offer exchange services between virtual assets and fiat currencies as early as 2016, being one of the first jurisdictions globally to enact such changes. The island also introduced specific requirements for entities wishing to undertake token issuances, publishing guidance in July 2018. Taking several steps back, in 1958, Jersey adopted its [Control of Borrowing \(Jersey\) Order 1958 \(COBO\)](#), which imposes a *consent requirement* on any entity wishing to raise capital in or from within Jersey. COBO grants the Jersey Financial Services Commission (**JFSC**) powers to impose whichever conditions it deems appropriate, yielding a level of control and visibility over all entities incorporated in the jurisdiction.
- 4 When granting a COBO consent to entities operating in the virtual assets industry, one of the conditions imposed by the JFSC is the requirement to appoint a locally licensed trust and company service provider (**TCSP**), which includes the requirement for a principal person (such as a director of the TCSP) to be appointed to the management function of the entity. By imposing this condition, the JFSC places the onus on TCSPs to ensure that such entities implement adequate systems and controls to manage and mitigate ML/TF risks arising from their activities.
- 5 Although the JFSC may have an element of control over all business activities in the jurisdiction, capacity building in this rapidly evolving sector has been slow, which is a global trend amongst authorities. The level of knowledge and understanding of virtual assets and the risks involved remains limited both at authority and entity level. Additionally, the JFSC and other relevant authorities are not currently collecting sufficient data that would allow them to further develop their understanding of the sector and the risks presented by its activities.
- 6 Given the limited data currently available to undertake an in-depth NRA focusing on the virtual asset sector in Jersey, this risk overview was conducted at a high level, considering the general ML/TF risks prevalent in the sector. This is a positive step for Jersey to identify, assess, and understand both, the virtual asset sector and the ML/TF risks it presents, as

well as to identify gaps in its current regime and consider any necessary legislative developments.

- 7 The virtual asset sector in Jersey remains small, with two operational virtual currency exchanges and a single custodian registered with the JFSC as of March 2022. There is also limited exposure stemming from other sectors including TCSPs and funds, which are indirectly exposed to entities that deal with virtual assets directly.
- 8 The GoJ and all other relevant authorities should seek to deepen their understanding of the virtual asset sector and to develop a legislative and regulatory regime that is fit for purpose to effectively monitor the sector and manage the risks the jurisdiction is exposed to in line with the FATF Standards.

## Introduction

- 9 The Bailiwick of Jersey is a self-governing Crown Dependency and a well-known international financial centre (**IFC**). Jersey's economy is significantly contributed to by its financial services sector, which, after the GoJ, is the Island's biggest employer. Deposit-taking businesses (banks), trust and company service providers, fund managers, and fund administrators dominate Jersey's financial services sector.
- 10 The GoJ undertook its first Money Laundering and Terrorist Financing National Risk Assessments throughout 2019 and 2020 and published reports in September 2020 and April 2021, respectively. The risk of ML was assessed at national and sectoral level and TF was assessed at national level; however, the assessments did not extend to the virtual asset sector.
- 11 One of the challenges faced when undertaking Jersey's initial ML and TF National Risk Assessments was the lack of available uniform data across sectors. This challenge was also faced when undertaking this high-level risk overview. Nevertheless, authorities in Jersey are now collecting more regular, sufficient, and uniform data through a single mechanism to allow ongoing detailed analysis of ML and TF risks, which will make future assessments more efficient, timely, and accurate. Also, the GoJ will undertake a more detailed risk assessment of the sector once Jersey's policy response is developed and new legislative requirements are in place, which will enable authorities to gather more granular data about the sector and its potential risks.

## Background

- 12 The FATF is an intergovernmental body responsible for the development of international standards, which it calls Recommendations<sup>1</sup>, for anti-money laundering (**AML**), countering the financing of terrorism (**CFT**), and countering the proliferation financing of weapons of mass destruction (**CPF**). It also promotes the implementation of measures to combat ML, TF, and PF.
- 13 FATF's first Recommendation requires countries to identify, assess, and understand the ML, TF, and PF risks within their jurisdiction, and to implement measures to mitigate the risks identified effectively.
- 14 The FATF began analysing virtual assets as early as 2014; however, it wasn't until October 2018 that it formally brought them under the scope of its Recommendations. Since then, the FATF has issued interpretive notes to Recommendations 15 (new technologies) and 16 (wire transfers) and has published guidance to assist countries and entities in applying a

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<sup>1</sup> [FATF Recommendations](#)

risk-based approach to virtual assets (VAs) and VASPs. The Interpretive Note to Recommendation 15 states: *In accordance with Recommendation 1, countries should identify, assess, and understand the money laundering, terrorist financing and proliferation financing risks emerging from virtual asset activities and the activities or operations of VASPs.* This high-level risk overview seeks to achieve this aim and to inform the jurisdiction's next steps regarding mitigating measures, including its policy response to deal with VAs and VASPs.

- 15 The FATF continues to actively monitor the implementation of standards related to VAs and VASPs in countries worldwide and has in place a contact group of public and private sector stakeholders who provide feedback on implementation and policy proposals for future amendments in this rapidly changing area. Jersey interacts with this work through its regular engagement with the FATF in a variety of areas.

## Scope

- 16 This risk overview considers the VA and VASP ML and TF risks in Jersey. It is based on available data and measures taken as of March 2022 by the GoJ and the JFSC, which are relevant to VAs and VASPs.
- 17 The key objective of this risk overview is to inform policy decisions for Jersey's legislative and regulatory approach to entities providing services relating to VAs and VASPs.

## Virtual assets and virtual asset service providers

- 18 This high-level risk overview is drafted in the context of AML/CFT requirements and is therefore driven by the FATF's definition of VAs which determines which assets fall within scope of its Standards. The FATF established the term *virtual assets* and consequentially *virtual asset service providers* and defines them as:
  - 19 Virtual asset: a digital representation of value that can be digitally traded, or transferred, and can be used for payment or investment purposes. VAs do not include digital representations of fiat currencies, securities, and other financial assets that are already covered elsewhere in the FATF Recommendations.
  - 20 Virtual asset service providers: 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:
    - a) exchange between virtual assets and fiat currencies;
    - b) exchange between one or more forms of virtual assets;
    - c) transfer<sup>2</sup> of virtual assets;
    - d) safekeeping and/or administration of virtual assets or instruments enabling control over virtual assets; and
    - e) participation in and provision of financial services related to an issuer's offer and/or sale of a virtual asset.
- 21 Not all entities that interact with VAs are deemed to be VASPs. Nevertheless, the FATF's definitions of VAs and VASPs are broad, and, as clarified in its October 2021 updated

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<sup>2</sup> *In this context of virtual assets, transfer means to conduct a transaction on behalf of another natural or legal person that moves a virtual asset from one virtual asset address or account to another.*

guidance<sup>3</sup>, these definitions are intended to be interpreted expansively. This means that a case should not exist whereby a relevant financial asset is not covered by the FATF Standards either as a VA or as another financial asset.

- 22 Some challenges exist concerning the terminology and definitions adopted to refer to VAs in different countries. Some of the most common terms used include cryptocurrencies, crypto-assets, digital assets, and virtual assets; however, these cannot always be used interchangeably as they do not necessarily represent the same concept.

### Virtual asset users

- 23 VA users can be categorised in three main groups; individuals such as retail investors or natural persons transacting using VAs, corporate users such as firms holding or investing in VAs or transacting using VAs (not on behalf of customers), and merchants, who may be firms or individuals that accept VAs as payment for products and services.



Individuals



Corporate users



Merchants

### VA state of play

- 24 VA adoption continues to rise globally with major players entering the space and making VA-related services available to an ever-growing customer base<sup>4</sup>. At the time of writing there are 18,223 known VAs with a total market value of \$1.7T<sup>5</sup>.
- 25 The chart below depicts the total market value of VAs globally, including stablecoins and other tokens between 29 April 2013 and 15 March 2022.



Source: [Coin Market Cap](#) March 2022

<sup>3</sup> FATF, [Guidance for a risk-based approach for VAs and VASPs](#), 28 October 2021

<sup>4</sup> [Triple A](#) estimates global crypto ownership rates average at 3.9%, with over 300 million VA users worldwide. It also estimates that over 18,000 merchants now accept VAs as payment.

<sup>5</sup> [Coinmarketcap](#), [Global Cryptocurrency Charts](#) , retrieved 15 March 2022

- 26 VAs have the potential to bring significant improvements to payment services by, for example, reducing the cost of basic payments and simplifying existing processes such as those for clearing and settlement. VAs may also help address financial exclusion, making financial services accessible to many of those currently underserved.
- 27 Although VAs are typically issued on public distributed ledgers where a clear audit trail of their movements can be followed, several factors make these types of assets vulnerable to use for nefarious purposes. Similar to traditional means of payment, VAs can be used for illicit activity and are exposed to ML and TF risks at every level of the money laundering process. According to the Basel Institute on Governance<sup>6</sup>, the predominant crimes involving VAs are not those that use VAs to launder the proceeds of crime or corruption. Rather, these are crimes that generate profits in VAs such as trade in drugs and other illicit goods on the dark web, ransomware, kidnapping and ransom payments, and cybercrime. This means that legitimately obtained VAs can then be used by individuals to purchase or procure illicit goods and services. Criminals that receive payment in VAs then attempt to transfer their illicit gains out of VAs and into fiat, which is where the money laundering offence takes place.
- 28 VAs can facilitate value transfers between two parties without the need for an intermediary, providing a mechanism for funds to be exchanged across borders at much higher speeds than traditional assets. This may also confer the ability to circumvent due diligence or sanctions screening in jurisdictions without a full regulatory regime for this sector.
- 29 Some of the factors that make VAs vulnerable to ML/TF risks include:
- a) the pseudonymous nature of users;
  - b) the ability to transact between parties without a trusted intermediary and without any customer due diligence checks or processes being conducted;
  - c) the ability to transact between parties without any transaction monitoring taking place;
  - d) the ability to establish non-face-to-face business relationships between VASPs and customers;
  - e) the cross-border nature of VA transactions; and
  - f) the speed at which value can be transferred globally.

### **VA capabilities & common illicit practices involving VAs**

- 30 Some of the known ML/TF practices relating to VAs include:

#### **Peer-to-peer networks**

The decentralised nature of many VAs has provided criminals with a mechanism to trade directly with one another and do so remotely and anonymously. As stated in the section above, an example of this is the use of dark web markets, where criminals can receive payment in VAs for the sale of illicit goods in and from unhosted wallets.

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<sup>6</sup> Basel Institute on Governance, *Cryptocurrencies and money laundering investigations*, 6 August 2021



### VA ATMs

VA automatic teller machines (**ATMs**) provide an attractive option for criminals looking to launder cash. Historically, crypto ATMs have applied little or no due diligence on customers, allowing criminals to launder funds whilst remaining anonymous.

### Mixers/tumblers

Mixers<sup>7</sup> or tumblers are used to obscure transactions by linking them in the same address and transferring them together in a way that makes them appear to have come from a different address. This provides an effective way for criminals trying to distance themselves or hide the source of a transaction.

### Unregulated exchanges

Given that not all jurisdictions have introduced regulatory frameworks for business activities involving VAs, VASPs have been able to operate without the legal or regulatory requirement to apply AML/CFT measures to customers. Many jurisdictions are yet to introduce a framework for VASPs, meaning that there may be many VASPs operating completely unregulated. The lack of regulatory requirements in certain jurisdictions provides an opportunity for criminals to open multiple accounts and potentially convert illicitly obtained VAs into fiat, and to integrate fiat into the financial system.

### Prepaid cards

VAs can be traded on a peer-to-peer basis (directly between two parties). However, to date, VAs are only accepted as a means of payment by some merchants. As a result, criminals using VAs must convert these to fiat to be able to make purchases. Prepaid cards issued by electronic money institutions with no, or weak, customer due diligence measures have provided a suitable mechanism for criminals to spend their VAs.

- 31 Although VAs remain the asset of choice by criminals for certain unlawful activities<sup>8</sup>, in 2020 global VA-related crime fell from \$21.4bn (2.1% of all VA transaction volume in 2019), to \$10bn (0.34% of all VA transaction volume in 2020)<sup>9</sup>. To put these numbers into context, the United Nations<sup>10</sup> estimates that the amount of money laundered every year is around 2-5% of global GDP (\$800bn - \$2tn).

<sup>7</sup> The basic principle of mixers involves a number of people coming together and pooling their bitcoins. Individuals then take back bitcoins of the same value. These bitcoins are likely to have originated from a different source (or sources) than the ones they brought to the mixer.

<sup>8</sup> Europol (2021), *Internet Organised Crime Threat Assessment 2021*, Publications Office of the European Union, Luxembourg.

<sup>9</sup> Chainalysis – *The 2021 Crypto Crime Report*.

<sup>10</sup> United Nations Office on Drugs and Crime, <https://www.unodc.org/unodc/en/money-laundering/overview.html>, retrieved 12 January 2022

32 Types of VAs

Types of virtual assets	Description	Inherent risk
Utility tokens	<p>VAs that grant digital access to specific digital platforms and to current or planned products or services. Typically only accepted by the issuer or other users of a particular digital platform.</p> <p>Examples: Filecoin (FIL), Civic (CVC)</p>	<p><b>Low risk:</b></p> <p>Utility tokens may resemble vouchers and typically only offer holders access to certain platforms or products, meaning that these types of tokens are not easily traded. Utility tokens are not considered to provide an efficient mechanism to exchange or realise value, making them unattractive to criminals to launder illicit funds or fund terrorism.</p>
Payment/exchange tokens	<p>VAs that can be used as digital means of payment or exchange, subcategories include:</p>	
	<p>Pseudo-anonymous: used as a means of exchange or potentially as a store of value. Transactions are linked to a specific sender.</p> <p>Examples: Bitcoin (BTC), Litecoin (LTC)</p>	<p><b>Medium risk:</b></p> <p>Transactions with pseudo-anonymous VAs are linked to a wallet address; however, the address may not be linked to an individual. Given that transactions with pseudo-anonymous VAs are stored in the blockchain and provide a full audit trail of VA movements (where other anonymisation techniques are not employed), these types of VAs present a medium risk of ML/TF.</p>
	<p>Anonymous (privacy coins): VAs with inbuilt anonymity features. Used as a means of exchange or potentially as a store of value. Transactions are not linked to a specific sender.</p> <p>Examples: Monero, Dash, ZCash</p>	<p><b>High risk:</b></p> <p>Privacy coins prevent third parties from linking a VA wallet to an identity. Although privacy features are not always sought to undertake illicit activity, criminals favour anonymous VAs which make their exposure to ML/TF higher than other types of VAs.</p>

Types of virtual assets	Description	Inherent risk
	<p>Platform: used to access digital marketplaces and platforms. Also used as a means of exchange and potentially as a store of value.</p> <p>Examples: Ethereum (ETH), ERC20 tokens</p>	<p><b>Medium risk:</b></p> <p>Transactions with platform tokens are linked to a wallet address which is normally linked to an individual. These types of VAs present higher levels of usability than other VAs as they can facilitate transactions between platforms, and, as a result, offer higher liquidity.</p>
	<p>Asset-backed tokens (also known as stablecoins): VAs that purport to maintain a stable value by referencing more than one fiat currency, a commodity, or a basket of commodities and fiat currencies.</p> <p>Examples: Tether Gold (XURt)</p>	<p><b>Medium-high risk:</b></p> <p>Stablecoins offer high usability when compared to other VAs, which makes them attractive from an ML/TF perspective as they can be exchanged and transferred more easily than other tokens. Some stablecoins also have the potential for mass adoption, increasing their exposure to ML/TF risks.</p>
	<p>Fiat-backed tokens (also known as stablecoins): VAs that purport to maintain a stable value by referencing a single fiat currency.</p> <p>Examples: Tether (USDt)</p>	
Closed-loop tokens	<p>VAs used as a means of exchange within a closed system.</p> <p>Examples: World of Warcraft gold (video games)</p>	<p><b>Low risk:</b></p> <p>Closed-loop tokens can only be used within a specific virtual community and cannot be exchanged for other virtual assets or fiat. Their limited usability makes them unattractive as a means to launder illicit funds or to pay for illegal goods.</p>

33 Unlike the VAs described in the table above, security tokens do not fall under the FATF’s definition of VAs given that these types of assets are considered to be financial instruments and subject to relevant securities laws<sup>11</sup>.

<sup>11</sup> Due to the structuring of Jersey’s securities and investments regime, security tokens will be captured as a virtual asset in Jersey.

## Types of VASPs

- 34 The World Bank has defined eight types of virtual asset service providers, however two are not defined as VASPs by the FATF. Nevertheless, the entity categories defined in the following table may interact with VAs or VA systems.

Types of VASPs	Description	Inherent risk
Wallet providers/custodians	Service providers enabling the storage of public and private keys.	<p><b>Low risk:</b></p> <p>VA custodians are most vulnerable to ML/TF risks at the time of deposits and withdrawals in VAs as it is often challenging to verify that the assets are being deposited or withdrawn from addresses owned or controlled by the customer. Nevertheless, custody services alone do not offer an effective means to transfer illicit funds, for which the inherent risk stemming from this service has been rated as low risk.</p>
Exchanges	Service providers facilitating virtual asset transfers and exchanges (VA - fiat / fiat - VA / VA - VA).	<p><b>Medium risk:</b></p> <p>Centrally operated exchanges offering fiat-VA, VA - fiat or VA - VA exchange services are exposed to ML/TF risks as criminals may attempt to use these platforms to place, layer, and integrate the proceeds of crime. Nevertheless, the volumes exchanged through centralised exchanges tend to be small or medium, and in most cases, trading is done using an orderbook, which minimises opportunities for coordination between criminals.</p>
Payment processors & brokers, including orderbook exchanges & OTC desks	Service providers conducting payment processing /arranging transactions.	<p><i>Payment processors and brokers, including orderbook exchanges:</i></p> <p><b>Low risk:</b></p> <p>Trades against order books tend to be smaller when compared to trades via OTC desks and fiat deposits and withdrawals are normally only accepted from/to a bank account in the customer's name. Deposits and withdrawals in VAs present a higher risk, but given that transaction amounts tend to be smaller, the ML risk presented by these types of entities is rated as low.</p>

Types of VASPs	Description	Inherent risk
		<p><i>OTC desks:</i>  <b>High risk:</b></p> <p>Volumes traded on OTC desks tend to be higher than those traded using an order book. With higher liquidity levels and a wider range of VAs available to trade, institutional investors, hedge funds, and other large players trade using OTC desks rather than exchanges. OTC desks also offer higher anonymity and may facilitate one-off transactions that do not require the establishment of a business relationship.</p>
Asset management providers	Entities offering fund management / fund distribution.	<p><b>Low risk:</b></p> <p>Asset managers may facilitate access to VA investments as part of their fund management services. Asset managers will not be classified as VASPs unless they offer any of the five activities defined by the FATF as VASP services and who are not covered elsewhere in the regulatory regime. In terms of exposure to VAs, these types of entities are a step removed in the value chain, as they will typically access VAs via a VASP.</p> <p>Investing in funds may not be an attractive option to launder the proceeds of illicit activity as they tend to be longer-term strategies that do not offer an effective mechanism for criminals to layer funds and access them immediately. Where those strategies are not longer-term, the risk of this structuring being attractive or utilised to launder the proceeds of illicit activity may not be managed as effectively.</p> <p>There is a risk that asset managers may purchase VAs from unregulated exchanges, or exchanges with lax customer due diligence requirements.</p> <p>Also, one-off large transactions may increase the risk of ML; however, regulated asset managers are more likely to only deal with regulated exchanges.</p>

Types of VASPs	Description	Inherent risk
		<p>Given the degree of separation between VAs and fund managers, and the product's unattractiveness for ML/TF, we have assigned a low-risk rating to entities providing asset management services.</p>
Issuers	<p>Entities issuing and selling VAs to the public.</p>	<p><b>Medium risk:</b></p> <p>Although newly issued tokens may not offer a practical means to launder illicit proceeds, weak controls or lacking AML/CFT processes by issuers may allow criminals to purchase these tokens using criminal proceeds and hold them as a speculative investment. Newly issued tokens that are not easily converted into fiat or other VAs may not be attractive to criminals; however, given the inconsistency in approaches taken by issuers and regulators globally, we have rated this activity as presenting a medium risk of ML/TF.</p>
Investment/trading platforms	<p>Entities enabling investment in or the purchase of VAs via a managed investment scheme or a derivatives issuer providing VA options, or via a private equity vehicle that invests in VAs.</p>	<p><b>Low risk:</b></p> <p>Investment/trading platforms acting as an intermediary between their customers and either financial institutions (such as asset managers), or VASPs (such as exchanges or VA trading platform operators) are exposed to a low risk of ML/TF.</p> <p>Deposits by customers of these types of entities are normally only accepted if made from bank accounts under the customer's name, meaning that the funds reaching the investment/trading platform have already gone through AML/CFT checks by the bank.</p> <p>As with asset managers, the degree of separation between these types of entities and the VAs also decreases their exposure to ML/TF risks presented by the VAs they enable investment in.</p>

Types of VASPs	Description	Inherent risk
<b>Not covered by FATF Recommendations</b>		
Miners/validators/pool operators	Entities that validate and confirm transactions on a distributed ledger. Although not usually captured by the VASP definition, if they hold sufficient control/validation power, they could be considered VASPs.	<p><b>Low risk:</b></p> <p>These types of entities present a low risk of ML/TF given that these activities do not provide an effective mechanism to launder the proceeds of crime or fund terrorist activities.</p> <p>It should be noted that there are reports of State actors trying to use VA mining as a means to evade international sanctions.</p>
Technology and ancillary service providers	Entities offering mixing services, blockchain explorers, web administration, mining hosting services, information providers	<p><b>Low risk:</b></p> <p>Technology and ancillary service providers are exposed to a low or very low risk of ML/TF given that they are not involved in VA fund flows.</p>

- 35 The FATF has highlighted that the wide range of providers in the virtual assets space and their presence across several jurisdictions can increase the ML/TF risks associated with VAs and VA financial activities due to potential gaps in customer and transaction information. This is a particular concern when the following risk elements are present:
- a) transactions are cross-border;
  - b) there is a lack of clarity on which entities or persons (natural or legal) involved in the transaction are subject to AML/CFT measures; and
  - c) there is a lack of clarity regarding which countries are responsible for regulating (including licensing and/or registering) and supervising or monitoring those entities for compliance with their AML/CFT obligations.
- 36 Further, if a VA achieves sufficient global adoption by customers such that it is used as a medium of exchange and store of value without the use of a VASP or other regulated financial institution, the lack of AML/CFT controls and compliance monitoring could mean the VA is especially high risk.

## Token issuances

- 37 Token issuance refers to the process of creating new VAs and selling them to the public or adding them to the total supply of the VA in question. Initial Coin Offerings (**ICOs**) are one of the better-known use-cases for token issuances. ICOs are normally used by start-ups to raise funds for new projects, similar to crowdfunding; however, in ICOs, subscribers will invest fiat or VAs and receive newly created tokens in exchange. 2017 saw a significant surge in ICOs and, between January 2017 and October 2018, almost 800 ICOs were launched worldwide, raising around \$20bn<sup>12</sup>.
- 38 ICOs remain mostly unregulated, although several countries have now introduced registration or other authorisation frameworks for entities wishing to raise funds through an ICO. The lack of regulation and control over these types of entities has resulted in numerous scams and millions lost by investors.
- 39 Token issuances can also be made in the form of Security Token Offerings. Security tokens are programmable VAs that represent ownership interests in an asset. Security tokens are considered financial instruments in some countries given their specific characteristics and are therefore subject to relevant securities legislation in those countries. This is not the position in Jersey.
- 40 Token issuances are not always intended to raise funds, some companies issue tokens and distribute them as rewards to users. User purpose is often speculative with the hope that the tokens will increase in value.
- 41 International standards specific to token issuances are yet to be developed and there is a lack of consistency in the approach taken to issuers globally. This creates opportunities for regulatory arbitrage and increases the risk of fraud and other forms of financial crime.

## UK's approach to regulating VA activities

- 42 Traditionally, the UK market has provided opportunities for the Island's financial services sector. Over the last 50 years, Jersey has established a relationship with the City of London and there are strong links between businesses in the two jurisdictions<sup>13</sup>.
- 43 While Jersey has sought business opportunities in new markets including Asia, the Middle East, sub-Saharan Africa, and North America, the GoJ primarily considers policies adopted in the UK and EU when developing its own.
- 44 In January 2020, the Financial Conduct Authority (**FCA**) was designated as the AML/CFT supervisor for cryptoasset businesses in the UK. Cryptoasset businesses include custodian wallet providers and cryptoasset exchange providers offering exchange services between VAs and fiat and VAs and other VAs, including crypto ATMs, peer-to-peer providers, and issuers of cryptoassets.
- 45 The UK's registration process for cryptoasset businesses has been subject to significant delays, for which the FCA introduced a Temporary Registration Regime in December 2020 to allow cryptoasset businesses that were operational prior to 10 January 2020 to continue operating until their registration is determined. Cryptoasset businesses that were not operating prior to 10 January 2020 must become registered prior to commencing operations.

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<sup>12</sup> Forbes, *Where Did The Money Go? Inside the Big Crypto ICOs of 2017*, retrieved 1 December 2021

<sup>13</sup> Paragraphs 2.13 and 2.14 of the National Risk Assessment of Money Laundering of the Bailiwick of Jersey, September 2020



- 46 Although the UK's regime for cryptoasset businesses is an AML/CFT framework, registration and ongoing requirements also cover several prudential and conduct obligations. Cryptoasset businesses in the UK must comply with the requirements of the Proceeds of Crime Act 2002, the Money-Laundering and Terrorist Financing (Amendment) Regulations 2019 (**MLRs**), and other relevant legislation.
- 47 As part of the application for registration, firms are required to submit information to the FCA on their operations, business plan, marketing plan, structural organisation, systems and controls, and governance arrangements.
- 48 Between July and October 2021, Her Majesty's Treasury consulted on further proposed amendments to the MLRs. The proposed amendments would tailor the provisions of the EU's Fund Transfers Regulation to the cryptoasset sector, making VA transactions subject to information exchange requirements.

## EU's emerging regime for virtual assets

- 49 The European Union's Fifth Anti-Money Laundering Directive (**5AMLD**) was amended to introduce certain obligations on entities dealing with VAs in the EU. The VA-related activities brought within scope of AML/CFT requirements included exchange services between fiat currencies and VAs, and VA custody services. The amended 5AMLD came into force in July 2018 and EU Member States had until January 2020 to transpose the requirements into national law.
- 50 Although this was a first step to bring some VA activities within the scope of AML/CFT supervision, the requirements under the amended 5AMLD are not completely aligned to the FATF Standards. Further to the 5AMLD changes, the EU has classified VAs as either security tokens, payment tokens, or commodity tokens.
- 51 Security Tokens (financial instruments) fall under the scope of existing financial services legislation such as the Markets in Financial Instruments Directive (**MiFiD II**).
- 52 For payment tokens or commodity tokens not already caught under existing financial services legislation, the European Commission has introduced the proposed Markets in Crypto-assets Regulation (**MiCA**). It is intended that MiCA captures every VA that is not already covered by other frameworks and harmonises the approach to authorisation and supervision of entities providing services to these types of assets in the EU. MiCA introduces requirements for issuers of non-security tokens, including issuers of stablecoins, and for service providers conducting any of the following activities:
  - a) VA custody;
  - b) operating a VA trading platform;
  - c) exchange services of VAs for fiat currency and VAs for other VAs;
  - d) execution of orders for VAs;
  - e) placing of VAs;
  - f) reception and transmission of orders for VAs; or
  - g) providing advice on VAs.
- 53 MiCA is mostly aligned to the FATF Standards, although the way in which it defines a VASP (referred to as a CASP in MiCA) is not as broad as the FATF's definition. In its October 2021 updated guidance, the FATF clarified that its defined terms should be interpreted expansively. The guidance states that if an entity is involved in the launching and deployment of decentralised services, as well as any entity receiving fees, commissions,

spreads, or other benefits from VASP services, it could be caught under the definition of a VASP. MiCA introduces a straightforward disclosure regime for all covered activities (issuance of VAs, and CASPs) as well as more onerous conduct and prudential provisions for other (certain issuers and CASPs) activities.

- 54 MiCA is part of a broader virtual assets regime, which includes three additional pieces of EU legislation: the DLT Pilot Regime Regulation (**PRR**); the new Anti-Money Laundering Regulation package (**AMLRP**); and the Directive for Administrative Cooperation (**DAC8**, replacing DAC7).
- 55 MiCA, the PRR, AMLRP and DAC8 are the main pillars of the emerging VA market in the EU and are expected to influence the approach taken by other jurisdictions, potentially generating a global regulatory standard. These regulatory initiatives are part of a wider EU Digital Finance Strategy, announced in 2019. The EU Digital Finance Strategy includes the transition from open banking to open finance, the creation of a common area for supervisory data, a policy that defines the uses of AI in financial services, and the adoption of a new electronic identity regulation (e-ID that replaces the eIDAS) that allows pseudonymity, which is core in the DLT and blockchain applications.

#### **PRR**

- 56 The PRR introduces a regulated sandbox that will allow certain financial institutions to test the use of distributed ledger technology for trading, clearing, and settlement. This means that tokenised securities will be transacted, settled, and cleared using permissioned ledger venues.
- 57 Although the PRR and MiCA were introduced at the same time, the PRR has moved through the EU's legislative process more rapidly than MiCA and was adopted in December 2021. MiCA is expected to be finalised by Q3 2022.

#### **AMLRP**

- 58 The AMLRP consists of four main policies; an Anti-Money Laundering Regulation; an Anti-Money Laundering Directive (6AMLD, replacing 5AMLD); a Regulation to establish a new European AML Agency; and a dedicated Regulation for the transfer of VAs. The Regulation for the transfer of VAs will transpose some elements of the FATF's Recommendations into EU law and will provide the standards for uniform implementation across the EU. The AMLRP is expected to be adopted in Q3 2022.

#### **DAC8**

- 59 DAC8 was announced in July 2021, although no text has yet been introduced (expected between July and December 2022), it focuses on tax cooperation between entities and jurisdictions within the EU. The Directive is expected to include provisions for the tracking of investments and returns in VAs and oblige VA exchanges and other related entities to submit reports to Member States' tax authorities.
- 60 As previously mentioned, the GoJ considers EU policy when developing its own policy response to new business models and sectors therefore the forthcoming changes to EU legislation are being closely monitored.

## **Legislative and regulatory environment for VAs in Jersey**

- 61 Jersey has not adopted specific legislation to deal with VAs as defined by the FATF; however, the existing legislative and regulatory framework captures several related

activities such as exchange services between VAs and fiat currencies, token issuances for non-security tokens and security tokens, security token exchanges, VA custody, and funds investing in VAs or in VA businesses. At the time when this risk overview was undertaken, the GoJ considered that the policies and mitigation measures in place are sufficient to mitigate the most significant risks Jersey faces from its exposure to VAs and VASPs. Nevertheless, it recognises that more detail is required to understand the risk exposure at a more granular level and to implement a revised policy approach.

- 62 Although Jersey has not implemented specific comprehensive VA legislation, existing legislation imposes a *consent requirement* on any entity wishing to raise capital in or from within Jersey through the COBO. This gives the JFSC an element of visibility over all operations in Jersey. COBO grants powers to the JFSC to impose conditions on entities as and when required.
- 63 Guidance issued under COBO includes the JFSC's [Sound Business Practice Policy](#), under which entities that are involved with or deal with VAs are considered to be conducting a *sensitive activity* and must comply with certain more stringent AML/CFT provisions.

### Virtual currency exchanges

- 64 Jersey's main AML/CFT law is the [Proceeds of Crime \(Jersey\) Law 1999 \(POCL\)](#). In 2016, the POCL was amended by the [Proceeds of Crime \(Miscellaneous Amendments\) \(Jersey\) Regulations 2016](#) to introduce definitions for *virtual currency* and *virtual currency exchange*, among other changes. This specifies that the business of providing virtual currency exchange services to third parties is a financial services business subject to AML/CFT provisions.
- 65 As at March 2022<sup>14</sup>, the POCL defines virtual currency as any currency which (whilst not itself being issued by, or legal tender in, any jurisdiction)-
  - a) *digitally represents value;*
  - b) *is a unit of account;*
  - c) *functions as a medium of exchange; and*
  - d) *is capable of being digitally exchanged for money in any form.*
- 66 Virtual currency exchanges are defined as:
  1. The business of providing, to third parties, the service of virtual currency exchange, where the business is not otherwise included in this Schedule (Schedule 2 of the POCL).
  2. In this paragraph –
    - i. *virtual currency exchange* means the exchange of virtual currency for money in any form, or vice versa<sup>15</sup>; and
    - ii. a reference to providing a service to third parties shall not include a company providing that service to a connected company.

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<sup>14</sup> Legislation adopted by the States Assembly on 31 March 2022, expected to come in to force by the end of March 2023, will replace the definitions of virtual currency and virtual currency exchange with *virtual asset* and *virtual asset service provider*.

<sup>15</sup> Note that the definition of virtual currency exchange does not extend to exchanges of VAs for VAs. However, entities dealing with VAs will be considered to be conducting *sensitive activity* and subject to certain AML/CFT provisions.

- 67 Orders made by the Minister for External Relations and Financial Services under Article 37 of the POCL, such as the [Money Laundering \(Jersey\) Order 2008 \(ML Order\)](#), establish the preventative measures to be implemented by financial services businesses. In addition, the [Proceeds of Crime \(Supervisory Bodies\) \(Jersey\) Law 2008 \(POC \(Supervisory Bodies\) Law\)](#), establishes the registration requirements for specified financial services businesses.
- 68 Under the ML Order, relevant persons (as defined) must comply with recognised AML/CFT requirements, such as appointing a compliance officer, maintaining appropriate policies and procedures, undertaking customer due diligence, maintaining certain records, and reporting suspicious activity.
- 69 As a specified financial services business, Part 3 of the POC (Supervisory Bodies) Law requires that virtual currency exchanges apply to the JFSC for registration. The specific application requirements in the POC (Supervisory Bodies) Law are high-level. However, the JFSC has the power to require as much information as it deems necessary, in relation to determining an application, either through the designated application form or by written notice following submission of an application.
- 70 Once registered under the POC (Supervisory Bodies) Law an entity must comply with the regulatory requirements set out in the JFSC's [AML/CFT Handbooks](#), even though these do not yet include any references to VA / VASP activity<sup>16</sup>.

### Virtual asset custody

- 71 The [Financial Services \(Jersey\) Law 1998 \(FSJL\)](#) states that *a person carries on financial service business if, by way of business, the person carries on investment business, trust company business, general insurance mediation business, money service business, fund services business, or AIF services business.*
- 72 Acting as a trustee, custodian, or depositary in relation to an unclassified or unregulated fund is considered as undertaking fund services business under the FSJL. As it relates to VAs, if an entity is providing virtual asset custody services by way of business, whereby it safekeeps or controls VAs or the means of access to the VAs on behalf of an unclassified or unregulated fund, the entity is deemed to be carrying on fund services business and subject to regulation under the FSJL. Nevertheless, where an express trust is created to safeguard or control the assets on behalf of third parties, if the activity is by way of business, the entity would be treated as a trust and company service provider and subject to the relevant requirements under the FSJL.
- 73 Incidental or ancillary custody services may be exempt from provisions under the FSJL. For example, if registered virtual currency exchanges provide custody services to customers to allow access to their platforms, registration exemptions may apply as providing the custody service may be considered ancillary or incidental to the activity of being a virtual currency exchange.

### Token issuances

- 74 Whilst most token issuances are not regulated by the JFSC, all entities seeking to issue tokens in Jersey must comply with several requirements including being granted approval by the JFSC prior to undertaking any related activity.
- 75 The COBO is the relevant statutory instrument governing the raising of capital in Jersey, meaning that token issuers must comply with this Order. To establish a company, limited partnership, limited liability partnership or unit trust in Jersey a *COBO consent* must be

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<sup>16</sup> A position that will change for virtual currency exchange businesses on 31 May 2022 when the [Consolidated AML/CFT Handbook](#) becomes effective

sought, and the JFSC may impose conditions on entities when granting such consent. In addition to meeting the requirements under COBO, issuers must also comply with Jersey's Sound Business Practice Policy.

- 76 Issuers are required to be incorporated as a Jersey company and must be administered by a locally licenced TCSP, which is regulated by the JFSC and as such must comply with a wide range of regulatory requirements covering prudential and conduct of business as well as AML/CFT.
- 77 Regardless of the type of token being issued, through the COBO conditions applied, issuers must: apply relevant AML/CFT requirements to customers; produce a white paper (see also paragraph 80 point i)), and comply with investor protection obligations.

#### **Token classification**

- 78 When determining an application from a prospective issuer, the JFSC will consider the economic function and purpose of the tokens to classify them appropriately. Tokens will be classified as security tokens or non-security tokens, the latter typically being either utility tokens or cryptocurrency (payment) tokens.
- 79 The JFSC has issued a [guidance note on the application process for issuers of initial coin offerings](#). This is applicable to all issuers, regardless of the type of token being issued, however, the JFSC may choose to relax certain conditions for non-security token issuances. Additional conditions may also be included if necessary.
- 80 As at March 2022, general requirements for all issuers includes:
  - a) appointing an appropriately licensed TCSP that will provide a registered office address to the issuer;
  - b) being incorporated as a Jersey company;
  - c) being granted a COBO consent;
  - d) complying with the Sound Business Practice Policy;
  - e) applying relevant AML/CFT requirements to persons that purchase tokens or sell tokens back to the issuer;
  - f) appointing a Jersey resident director who is a natural person and also a principal person of the appointed TCSP;
  - g) complying with ongoing audit requirements;
  - h) implementing processes and procedures for investor protection;
  - i) preparing and submitting a white paper to the JFSC which is in line with the requirements under the [Companies \(General Provisions\) \(Jersey\) Order 2002](#); and
  - j) ensuring all marketing materials are fair, clear, and not misleading.
- 81 Requirements under the Sound Business Practice Policy include undertaking customer due diligence (**CDD**), transaction monitoring, and reporting of suspicious activity. Each TCSP appointed must be satisfied with the level of CDD undertaken by issuers.

#### **Security token exchanges**

- 82 Although there is no defined approach to deal with entities providing exchange services in relation to security tokens, the JFSC would consider applications by these types of entities on a case-by-case basis to capture them under the most appropriate regime. In any case, entities wishing to undertake this activity must obtain a COBO consent from the JFSC and will be subject to the provisions under the Sound Business Practice Policy.

- 83 When determining whether to grant a COBO consent, the JFSC will consider legal opinions and assessments undertaken by the entity. Entities providing security token exchange services will fall under the scope of the POCL.

### Fund Managers and Administrators

- 84 Fund managers and fund administrators of unclassified and unregulated funds must be registered by the JFSC as fund services businesses under Article 9 the FSJL. Fund managers and fund administrators (on behalf of the funds they act for) can invest in VAs and VA-related entities under their existing registration, and do not require additional permissions.
- 85 As previously mentioned, any activities relating to virtual assets are deemed to be sensitive activities under the Sound Business Practice Policy, and (regardless of the investment strategy and target fund assets) are subject to several AML/CFT requirements.

### Mining

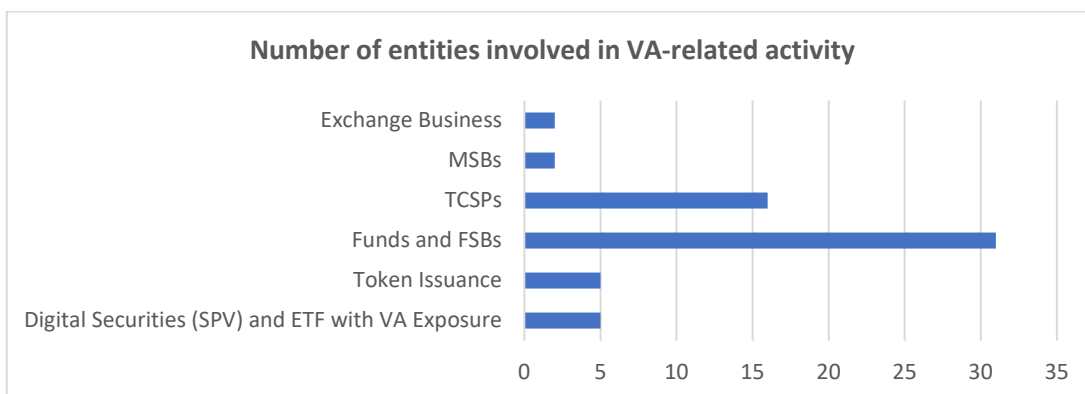
- 86 Mining activities are not currently under the scope of any specific framework in Jersey.

### Supervision

- 87 Part 2 of the POC (Supervisory Bodies) Law has the effect of making the JFSC the AML/CFT supervisory body in Jersey.

## Service providers with an exposure to virtual assets in Jersey

- 88 As of March 2022, information regarding the sizes and types of firms providing VA services in Jersey was not readily available in a structured format.
- 89 Some firms known to be operating in Jersey that provide VA-related services, or services with an exposure to VAs include:



- a) VA exchange services providers;
- b) Money Services Businesses (**MSBs**) (e-money and payment institutions that enable their users to deposit fiat and withdraw to and from different VASPs such as exchanges). It should be noted that in both instances these businesses are benefitting from an exemption from both the FSJL and requirements within POCL as a result of the [Financial Services \(Money Service Business \(Exemptions\)\) \(Jersey\) Order 2007](#) - a position under review as part of the ongoing scope exemptions work;

- c) TCSPs (provide administration and directorship services to issuers and other entities that provide VA-related services);
- d) Funds and Fund Managers and Fund Administrators (private funds and collective investment funds that facilitate investment in VAs), including VA custody providers (a single entity has been approved to provide VA custody services, and the company only services institutional investors);
- e) Token issuance – Jersey based issuers who have issued their own initial coin offerings or centralised utility-type VAs under the COBO. They are all required to adhere to the conditions identified within the ICO Guidance; and
- f) Digital Securities (SPV) and Exchange Traded Funds with VA Exposure – (a number of virtual asset themed “exchange traded product” platforms which have been granted with a consent to issue securities under the COBO. These platforms offer investors the ability to gain economic exposure to underlying pools of various VAs.

## Jersey’s ML & TF National Risk Assessments 2020 and 2021

- 90 Jersey’s AML/CFT framework is highly aligned to the FATF Standards, and the jurisdiction has implemented all relevant provisions contained in the key AML/CFT international instruments such as the Vienna and Palermo Conventions of 1998 and 2000. Nevertheless, as an IFC, Jersey’s exposure to cross-border threats is high and increases as Jersey seeks business opportunities in new jurisdictions. Also, as an IFC, Jersey is more likely to be exposed to the layering stage of ML, which typically involves banks, TCSPs, and funds, some of the jurisdiction’s largest and most important sectors.
- 91 Jersey’s initial ML National Risk Assessment rated the TCSP, investment, and funds/fund services businesses as presenting a medium-high residual risk of ML.
- 92 In relation to TF, when conducting its TF NRA, Jersey assessed its exposure on a national basis as opposed to on a sector-by-sector basis. Jersey’s most significant TF threat stems from entities that move funds through, or store funds in Jersey. The overall risk of Jersey being used as a conduit for TF was rated as medium-low.
- 93 Although this high-level risk overview is specific to the VA sector, we must consider the sectors that interact with VAs and VASPs most, to adequately assess the jurisdiction’s exposure to ML/TF risks from a VA perspective. The data available suggests that the main sectors in Jersey with an exposure to VAs are fund managers and TCSPs.
- 94 Jersey’s initial ML NRA identified a number of overarching residual risks, all of which are relevant for TCSPs, funds/fund services businesses and which have resonance with the findings of this VA risk overview:
  - *understanding by authorities of ML risk not developed to a sufficient granular level to fully understand ML risk in key market sectors;*
  - *available data collected is not uniform or sufficient to monitor ongoing ML risk;*
  - *for both authorities and industry, there is not a fully developed understanding of the risk specific jurisdictions pose to Jersey in respect of cross-border ML risk;*
  - *policy development is not sufficiently resourced or agile enough to fully develop and coordinate a policy response to emerging threats faced by Jersey as an IFC;*

- *law enforcement agency cooperation with jurisdictions where common predicate offences occur still requires development to pursue effective ML investigations and prosecutions in Jersey;*
- *for both authorities and industry, the understanding of specific topics relevant to ML is still developing and is uneven in key industry sectors most exposed to those risks – this is exacerbated by the limited understanding of ML risk in common foreign markets with which Jersey interacts. Specific topics of note are PEPs, complex structures, and specific funds ML risk;*
- *the quality of intelligence available to the FIU, combined with processing challenges and resource constraints means that Jersey has yet to fully resource financial crime investigation. It therefore remains challenging to identify, investigate, and prosecute ML in areas that present the greatest threat to Jersey such as cross-border ML threat. This is exacerbated by foreign cooperation risks;*
- *the effectiveness of tax enforcement and cooperation may indicate challenges in identifying and investigating tax evasion as a common predicate offence presenting a risk to Jersey’s significant sectors;*
- *the supervisory approach is not fully tailored to higher risk sectors and themes in order to effectively mitigate ML risk; and*
- *typologies of ML and guidance for specific important sectors, combined with outreach is required to ensure the industry fully understands the ML risk in those sectors.*

95 Regarding Jersey’s overall ML threat, the initial ML NRA identified that, measured by number and value, most of Jersey’s customer base consists of non-residents. This means that activities resulting in funds being held in Jersey largely take place outside the jurisdiction, as do most predicate offences. Proceeds of predicate offences are then potentially placed and laundered using Jersey firms.

96 Top criminality suspected in relation to foreign predicate offences relates to tax evasion, fraud, and corruption, with the greatest threat to Jersey stemming from non-residents seeking to hide the proceeds of corruption and white-collar crime in Jersey. Tax-related suspicions (mostly tax evasion) are in the top-three reported crimes suspected by Jersey firms. Relating to tax evasion, complex structures in Jersey have provided one possible mechanism to launder illicit proceeds generated outside of Jersey.

97 As it relates to domestic predicate offences, drug trafficking, fraud, and larceny are the most prevalent offences in Jersey.

98 The overall ML threat in Jersey was rated as medium-high, having assigned a higher weighting to foreign predicate offences, as these posed a much higher threat to the jurisdiction when compared to cross-border and domestic threats.

## Overall ML threat assessment and conclusion

ML Threat:	Foreign Predicate Offences	Cross-Border	Domestic	Overall
Rating	Medium-High	Medium	Medium-Low	Medium-High



- 99 Following publication of the ML and TF National Risk Assessments, authorities in Jersey have embarked on a National Financial Crime Work Programme, co-ordinated by the GoJ, consisting of over 100 actions covering areas such as risk understanding, risk mitigation, legislation, and regulation in order to address the NRA findings.

## Jersey’s contextual factors and impact on risk assessment

- 100 The following table sets out key contextual factors and their impact on the VA risk overview:

Contextual factors	Impact on VA risk overview
<b>Politics</b>	
<p>Jersey is a Crown Dependency and is not part of the UK. The UK is responsible for Jersey’s international affairs and defence; however, it will not act on Jersey’s behalf without prior consultation.</p> <p>Jersey’s government is led by a Council of Ministers consisting of a Chief Minister and 11 ministers who are elected by the Assembly of the States of Jersey (the <b>States</b>).</p> <p>Jersey has 12 parishes, each with a Connétable (head of the parish) with executive powers. Each Connétable represents their parish in the States and may speak and vote on all matters.</p> <p>The States is made up by 49 elected members who adopt legislation and scrutinise the Council of Ministers.</p>	<p>Jersey’s political system is stable; however, given the generally conservative approach to innovative products, the appetite to attract market disrupters may be limited. This could result in slower regulatory change than would be required in order to develop the understanding and regulatory expertise required to supervise this rapidly evolving sector.</p>
<b>Economy</b>	
<p>Jersey’s economy is based on financial services, with a small percentage of the main economic indicator (Gross Value Added) being contributed by public administration and construction. The financial services sector is the biggest employer in Jersey after the GoJ, and the jurisdiction is rated 57/116 in the 2021 Global Financial Centres Index.</p>	<p>The focus of the island’s economy on the financial sector and the intention to develop and cater for fintech will result in a threat and potential vulnerability if the regulatory capabilities are not scaled up to meet this focus.</p>
<b>Geography</b>	
<p>Jersey is a 122km<sup>2</sup> island located 22.5km off the north-west coast of France and 137km from the English coast.</p>	<p>Jersey’s size and geography create advantages when combatting illicit cross border movement of physical goods and people. The island sits between two stable jurisdictions.</p>

<b>Access to financial services</b>	
Access to financial services and financial education in Jersey are relatively high.	As mentioned, Jersey’s conservative social and political leanings present barriers to entry to innovative service providers, leading Jersey residents to turn to VA-related service providers outside of Jersey.
<b>Demography</b>	
Jersey’s estimated population is 103,367 <sup>17</sup> with 79% of its resident population being Jersey- or other British Isles-born, a further 16% being born in a European country, with only 5% of the population being from the rest of the world.	Jersey’s small population may present resource challenges, particularly when the expertise and skillset required relates to new industries.

- 101 Based on the contextual factors set out above, Jersey’s economic reliance on financial services and the generally conservative approach taken to innovation could result in a delayed response to building the knowledge and capacity to deal with new types of products and services. This presents a high risk given that certain entities could potentially exploit the general lack of understanding by authorities as well as gaps and uncertainty in current legislation.

## Current VA environment in Jersey / risk overview

- 102 In Jersey’s initial ML NRA, the data used to determine ML risks presented by different financial services sectors included the size of each sector, its share in the economy, and its importance to the Jersey economy. Despite Jersey being one of the first jurisdictions to bring virtual currency exchanges under the scope of AML/CFT legislation, and to introduce clear guidance for token issuances, the data used to determine these matters (sector Gross Value Added, average headcount, revenue, total number of beneficial owners and controllers, and total assets under management) was not systematically available for the VA sector when conducting this high-level risk overview.
- 103 From the limited data available, the VA sector's size, share in the economy, and importance continues to be relatively small. This may be a result of the typically conservative approach taken by Jersey authorities and the jurisdiction's financial services sector.
- 104 The main types of entities interacting with VAs in Jersey are funds and fund managers that invest in VAs or in VA businesses and TCSPs that provide company administration and directorships to VA entities. These entities deal mainly with institutional clients outside Jersey. Whilst Jersey’s retail market is fundamentally non-existent, with limited apparent interest in VAs, there is evidence that islanders are beginning to have an interest in VA products as evidenced by some falling foul of cryptocurrency scams<sup>18</sup>. There does not appear to be any exposure to privacy coins.

<sup>17</sup> Taken from the 2021 census information available from [2021 census results \(gov.je\)](https://www.gov.je/2021-census-results).

<sup>18</sup> [Fraud hits £300k in months amid scammers' new crypto focus | Bailiwick Express](#)

- 105 Given the lack of a developed sector, Jersey's VA and VASP threat exposure is difficult to accurately identify and quantify although it is likely to be low given the perceived level of current activity.

## Mitigating measures

- 106 Jersey's amendment of its main AML/CFT legislation in 2016 brought virtual currency exchange businesses within the regulatory scope, this includes registration/notification with the JFSC, as well as standard AML/CFT obligations (such as suspicious activity reporting, undertaking CDD and appointing a money laundering compliance officer and reporting officer). However, the level of supervision and regulatory reporting that these types of entities are subject to would benefit from more clarity. Further clarity for entities involved with virtual assets will be achieved through the Proceeds of Crime (Amendment No. 6) (Jersey) Law 202- which introduces into Jersey legislation a definition of VAs and VASPs, in line with the FATF definitions, and brings them fully into AML/CFT regulatory scope through Schedule 2 to the POCL<sup>19</sup>.
- 107 The COBO consent requirement gives the JFSC the ability to impose conditions on entities wishing to raise capital in or from within Jersey. All activities involving VAs have been deemed as sensitive activities subject to the provisions in the Sound Business Practice Policy and must meet certain AML/CFT obligations stemming from COBO conditions. One of the COBO conditions imposed by the JFSC has been the requirement to appoint a locally licensed TCSP, with a principal person (such as a director of the TCSP) being appointed to the management function of the entity. By imposing this condition, the JFSC places the onus on TCSPs to ensure that such entities implement adequate systems and controls to manage and mitigate ML/TF risks arising from their activities.
- 108 Consequently, in Jersey, activities relating to VAs are directly or indirectly within the scope of AML/CFT legislation.
- 109 Through discussions it is understood that deposit-takers in Jersey have not provided banking services to entities that provide VA services. This means that Jersey entities wishing to interact with VAs must seek banking arrangements outside of Jersey. This is not saying that no customer of a Jersey registered deposit-taker has an exposure to virtual assets, simply that their general approach has helped to mitigate AML/CFT risks posed by VA-related activities. The cautious stance means that interest in the jurisdiction as a hub for these types of entities has been limited.
- 110 As part of their risk management framework, some authorised service providers in Jersey have introduced the use of blockchain analytics tools when conducting monitoring. These entities have also been proactive in implementing measures to address their AML/CFT risk exposure stemming from their use of, or involvement with, VAs. This can be seen as a positive approach by firms to mitigate their risk exposure.
- 111 Given the limited numbers of entities providing VA services in or from within the jurisdiction, the risk can be considered as low.

## Residual risk

- 112 The Jersey VA and VASP regime is not yet fully aligned to the FATF Standards. The level of supervision and regulatory reporting to which some of these types of entities are subject would benefit from further clarity. Without adequate oversight, the JFSC is unable to verify whether there are any deficiencies in the implementation of AML/CFT requirements by

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<sup>19</sup> The Amendment is expected to come into force by the end of March 2023.

firms. Also, the lack of legislative and regulatory certainty with regards to certain VA activities could lead to entities finding loopholes, potentially allowing them to operate under the radar. Nevertheless, once the Proceeds of Crime (Amendment No. 6) (Jersey) Law 202- is in force, it will bring VASPs fully within scope of AML/CFT provisions and will enable the JFSC to collect relevant data. This will also enable authorities to undertake a full risk assessment applying the World Bank methodology, in line with previous NRAs.

- 113 While the jurisdiction's conservative approach to VAs has served in some ways as a mitigating factor, it has also discouraged authorities and firms from developing a deeper understanding of the sector and the risks presented by VAs. A lack of experience and knowledge of the sector presents a high risk from a ML/TF perspective, as both authorities and firms that interact with VAs may be ill equipped to adequately address the risks to which they are exposed. It is unclear whether the TCSPs or other licensed entities have the necessary knowledge and understanding required to properly fulfil their requirements relating to implementation of adequate systems and controls and completion of ML/TF risk assessments.
- 114 The strategy for the development of capacity building within the jurisdiction is progressing, however, Jersey is currently more likely to follow a reactive rather than a proactive approach, heightening the risks presented by this emerging sector.

## Conclusion

- 115 The GoJ and all other relevant authorities should seek to deepen their understanding of the virtual asset sector and to develop a legislative and regulatory regime that is fit for purpose to effectively monitor the sector and manage the risks the jurisdiction is exposed to in line with the FATF Standards.
- 116 The GoJ is taking positive steps to identify, assess, and understand the ML and TF risks prevalent in the VA sector. It is also looking to identify gaps in its existing frameworks to inform legislative policy and develop a strategy to address those gaps effectively, in line with the FATF Standards.
- 117 The VA sector in Jersey remains small, meaning that the risks relating to ML/TF that it presents to the jurisdiction are perceived to be limited in terms of size and impact. The assessment of the true level of risk is hampered by the lack of available data on the sector. Going forward, planned legislative developments will see a more uniform approach in relation to data collection. This will allow for a more in-depth assessment of the risks presented by VAs in the jurisdiction and the assignment of a risk level or rating reflecting this.
- 118 It is important to note that this sector is rapidly evolving and with it the risks it presents, and therefore the potential risks need to be kept under constant review.