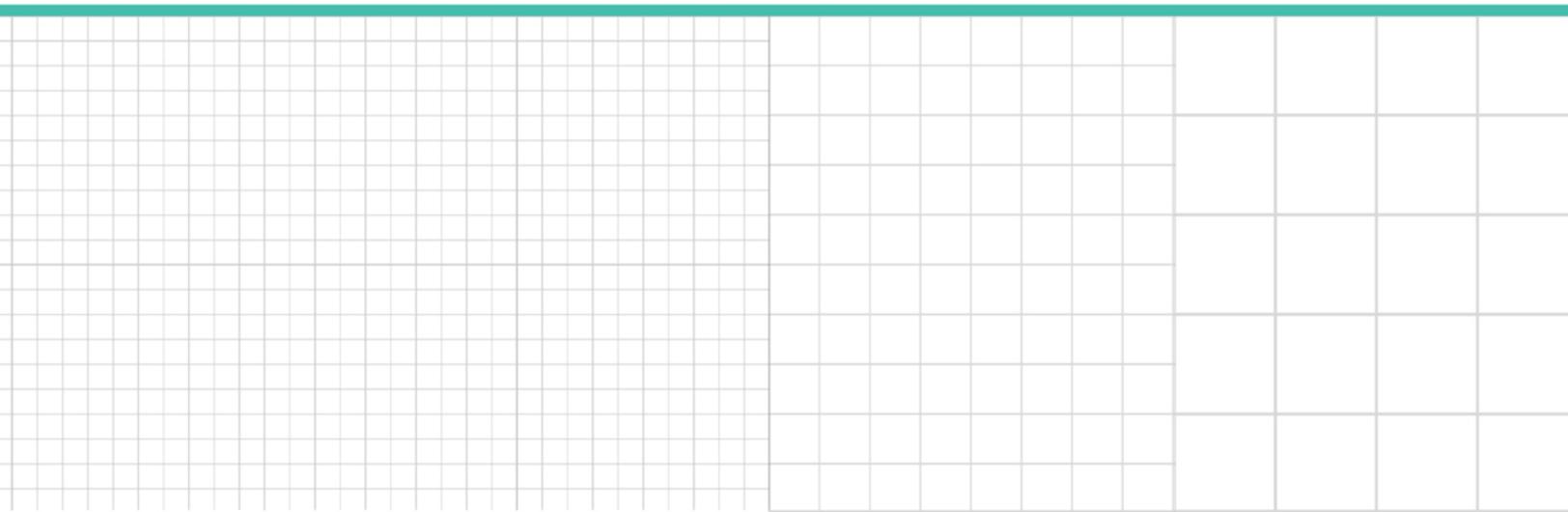


Professional Perspective

New FinCEN Guidance for Cryptocurrency and Blockchain Businesses

*Laura Jehl, Robert Musiala, Jonathan Forman,
and Joanna Wasick, BakerHostetler*

Reproduced with permission. Published May 2019. Copyright © 2019 The Bureau of National Affairs, Inc.
800.372.1033. For further use, please visit: <http://bna.com/copyright-permission-request/>



New FinCEN Guidance for Cryptocurrency and Blockchain Businesses

Contributed by [Laura Jehl](#), [Robert Musiala](#), [Jonathan Forman](#), and [Joanna Wasick](#), [BakerHostetler](#)

On May 9, 2019, the Financial Crimes Enforcement Network published [FIN-2019-G001](#), which provides new guidance on the application of the Bank Secrecy Act (BSA) and FinCEN regulations to money services businesses that engage in money transmission involving convertible virtual currencies.

While stating that it “does not establish any new regulatory expectations or requirements,” the guidance consolidates existing guidance, and in some areas applies the existing guidance to common business models and activities in ways that clarify how FinCEN intends to treat these activities going forward. The following is a summary of this important new guidance as organized by its six sections.

Key Concepts

Facts and Circumstances. The guidance emphasizes that “[w]hether a person is a money transmitter* under FinCEN’s regulations is a matter of facts and circumstances.” In applying MSB requirements, FinCEN will look to the facts and circumstances of the activity at issue, not the “label” used to describe the activity. Where a specific business model contains different features than those described by the guidance, different interpretations of the guidance may apply.

The guidance notes that “a person who is engaged in more than one type of business model at the same time may be subject to more than one type of regulatory obligation or exemption.” For example, developers or sellers of software applications and new CVC platforms may have different obligations related to their various roles in creating, selling, and using an application or CVC platform.

Broad Scope. The guidance provides an overview of key definitions and highlights the broad scope of money transmission as activity involving transmission of “currency, funds, or other value that substitutes for currency ... by any means,” including value “created ... originally for another purpose but then repurposed to be used as a currency substitute” The guidance makes clear that CVC falls into this broad definition of value, regardless of the label (e.g., “digital currency,” “cryptocurrency,” “cryptoasset,” “digital asset”) and regardless of the type of technology used in transmission of the value.

General Application of BSA Regulations to Money Transmission

Activity-Specific. The guidance reinforces that activities, not “formal business status,” will determine whether a person is an MSB. Notably, the guidance highlights that “a person is still a money transmitter ... if the person transmits value first, and only later accepts corresponding value ...” The guidance also highlights that a person may be a money transmitter when operating either on a transactional basis (e.g., with no expectation of an ongoing relationship), on an account basis (e.g., transacting with an established customer), or with the intent of transmitting value only under certain conditions.

Exclusions from Money Transmitter Definition. The guidance reviews certain activities that are exempt from the “money transmitter” definition, including providers of “delivery, communication, or network access services used by a money transmitter,” payment processors, operators of clearing and settlement systems, physical transporters (e.g., an armored car), prepaid access providers, and a person who “accepts and transmits funds only integral to the sale of goods or the provision of services, other than money transmission services, by the person who is accepting and transmitting the funds.” The guidance notes that “FinCEN interprets these exemptions strictly.”

BSA Obligations of Money Transmitters. The guidance provides an overview of the key obligations of money transmitters under the BSA. These include a culture of compliance; an AML Program consisting of appropriate policies, procedures and internal controls; a designated BSA compliance officer; ongoing training; and periodic independent review of the AML

* FinCEN’s regulations define the term “money transmitter” to include a “person that provides money transmission services,” or “any other person engaged in the transfer of funds.” A “transmittor,” on the other hand, is “[t]he sender of the first transmittal order in a transmittal of funds. The term transmittor includes an originator, except where the transmittor’s financial institution is a financial institution or foreign financial agency other than a bank or foreign bank.” In other words, a transmittor initiates a transaction that the money transmitter actually executes (See [FIN-2019-G001](#), p. 3).

Program. The guidance highlights the importance of taking a risk-based approach to BSA compliance, including a “well-developed risk assessment” that provides MSBs with a “comprehensive analysis of their individual risk profile.” The guidance clarifies that “transactions involving CVC qualify as transmittals of funds, and thus may fall within the Funds Travel Rule,” which requires money transmitters to provide certain information on senders and recipients of funds.

Application of BSA Regulations to Money Transmission Involving CVC

Prior Guidance–2011 MSB Rule. Before discussing specific CVC business models, the guidance discusses the 2011 MSB Final Rule that “made clear that persons accepting and transmitting value that substitutes for currency, such as virtual currency, are money transmitters.” The guidance highlights that MSB requirements “apply equally to domestic and foreign-located CVC money transmitters doing business in whole or in substantial part within the United States, even if the foreign-located entity has no physical presence in the United States.”

Prior Guidance–2013 VC Guidance. The guidance also discusses FinCEN's 2013 VC Guidance, which provided definitions of a CVC “exchanger,” “administrator,” and “user,” and clarified that “exchangers and administrators generally qualify as money transmitters under the BSA, while users do not.” The guidance highlights that “the method of obtaining virtual currency ... does not control whether a person qualifies as a ‘user,’ an ‘administrator’ or an ‘exchanger’” and that FinCEN interprets the term “another location” broadly in the context of CVC exchangers and administrators.

Guidance on Application of BSA Regulations to Common Business Models Involving the Transmission of CVC

P2P Exchangers. According to the guidance, “Peer-to-Peer (P2P) exchangers are (typically) natural persons engaged in the business of buying and selling CVCs. P2P exchangers generally advertise and market their services through classified advertisements, specifically designed platform websites, online forums, other social media, and word of mouth.” The guidance highlights that P2P exchangers are money transmitters. However, the guidance notes that an exemption may exist for persons engaging in P2P exchange activity “on an infrequent basis and not for profit or gain.”

CVC Wallets. The guidance describes CVC wallets as “interfaces for storing and transferring CVCs” and notes that there are different types of wallets, including “mobile wallets, software wallets, and hardware wallets,” as well as “hosted wallets” controlled by third parties and “unhosted wallets” where users control the funds.

“Hosted” Wallets. With respect to “hosted wallets,” the guidance explains that the host must comply with applicable requirements based on whether the wallet owner is a “user” under the [2013 VC Guidance](#), an agent of the host, or a financial institution that is not an agent of the host. These requirements include, respectively, procedures such as verifying and monitoring a user's identity and profile, monitoring agent activities, and complying with requirements applicable to correspondent accounts. The guidance notes that in some situations, the host may be required to comply with the Funds Travel Rule, “regardless of whether the regulatory information may be included in the transmittal order itself or must be transmitted separately.”

“Unhosted” Wallets. The guidance describes “unhosted wallets” as “software hosted on a person's computer, phone, or other device” that “do not require an additional third party to conduct transactions.” The guidance indicates that persons transacting through “unhosted wallets” on their own behalf are not money transmitters.

Multi-Sig Wallets. The guidance addresses the case of multi-signature (“multi-sig”) wallet providers that create wallets requiring more than one private key to effect transactions. According to the guidance, where a multi-sig wallet provider “restricts its role to creating un-hosted wallets that require adding a second authorization key ... the provider is not a money transmitter.” However, if a person “combines the services of a [multi-sig] provider and a hosted wallet provider, that person will then qualify as a money transmitter.” The guidance indicates that multi-sig providers will also be deemed money transmitters where they represent hosted value as account entries, interact directly with the payment system, or maintain independent control of the hosted value.

CVC Kiosks. The guidance makes very clear that owner-operators of “CVC automated teller machines (ATMs)” are money transmitters.

DApps. The guidance describes DApps as “software programs that operate on a P2P network of computers running a blockchain platform (a type of distributed public ledger that allows the development of secondary blockchains), designed such that they are not controlled by a single person or group of persons (that is, they do not have an identifiable administrator).” The guidance notes that “regardless of whether they operate for profit” DApps that accept and transmit value are money transmitters, and indicates that owners/operators of a DApp, or both, may also be considered money transmitters.

Anonymity-Enhanced CVC Transactions. The guidance clarifies that CVC transactions “structured to conceal information” or denominated in “types of CVC specifically engineered to prevent their tracing” (i.e., privacy coins) do not change the regulatory obligations of money transmitters.

Anonymizing Services Providers. The guidance makes clear that a CVC “anonymizing services provider” (e.g., providers of “mixers” or “tumblers”) is a money transmitter. The guidance states that CVC anonymizing services providers are not eligible for the MSB “integral exemption.”

Anonymizing Software Providers. According to the guidance, while an “anonymizing software provider” is not a money transmitter, “a person that utilizes the software to anonymize the person’s own transactions will be either a user or a money transmitter, depending on the purpose of each transaction.” Here the guidance notes that “originating or intermediary financial institutions that replace the proper identity of a transmitter or recipient in the transmittal order with a pseudonym or reference that may not be decoded by the receiving financial institution (i.e., substituting the full name of the transmitter with a numeric code) are not complying with their obligations under the Funds Travel Rule.”

Providers of Anonymity-Enhanced CVCs. Addressing so-called “privacy coins,” the guidance indicates that centralized “privacy coin” CVC payment systems will be deemed money transmitters, as well as persons who use “privacy coin” CVCs “to accept and transmit value from one person to another person or location.” The guidance indicates that developers of decentralized CVC payment systems will be deemed money transmitters if they “engage as a business” in transmitting value denominated in CVC.

Transmitters of Anonymity-Enhanced CVCs. With respect to “money transmitters that accept or transmit anonymity-enhanced CVCs,” the guidance indicates that compliance challenges may arise related to the Funds Travel Rule. According to the guidance, “[w]hen knowingly accepting anonymity-enhanced CVCs (or regular CVC that has been anonymized), money transmitters engaged in CVC transactions subject to the Funds Travel Rule must not only track a CVC through the different transactions, but must also implement procedures to obtain the identity of the transmitter or recipient of the value.”

CVC Payment Processors. The guidance clarifies that “CVC payment processors fall within the definition of a money transmitter and are not eligible for the payment processor exemption because they do not satisfy all the required conditions for the exemption.” This is because CVC payment processors do not “operate through clearance and settlement systems that admit only BSA-regulated financial institutions.”

CVC Money Transmission by Internet Casinos. According to the guidance, “Internet casinos” include “predictive markets, information markets, decision markets, idea futures, and event derivatives.” The guidance indicates that to the extent an entity of one of these types “accepts and transmits value denominated in CVC” the entity may be deemed a money transmitter.

Specific Business Models Involving CVC Transactions that May be Exempt From the Definition of Money Transmission

CVC Trading Platforms and Decentralized Exchanges. Consistent with the exemption for providers of “delivery, communication, or network access services used by a money transmitter,” the guidance indicates that a CVC trading platform or decentralized exchange that “only provides a forum where buyers and sellers of CVC post their bids and offers (with or without automatic matching of counterparties), and the parties themselves settle any matched transactions through an outside venue (either through individual wallets or other wallets not hosted by the trading platform)” will not be deemed money transmitters. In contrast, “if, when transactions are matched, a trading platform purchases the CVC from the seller and sells it to the buyer” the platform/exchange will be deemed a money transmitter.

ICO Issuers. The guidance makes clear that “[w]hether an ICO is subject to BSA obligations is a matter of facts and circumstances.” The guidance goes on to discuss two types of ICOs, noting that it “does not attempt to address every possible ICO business model.”

ICO Sales to Distinct Buyers. The first type of ICO business model addressed by the guidance involves scenarios where “exchange of CVC for another type of value may be instantaneous or deferred to a later date” and where value received will be used in whole or in part to develop the CVC or a related application or platform. According to the guidance, in this scenario “the seller of the CVC is a money transmitter, acting in the role of administrator, because at the time of the initial offering the seller is the only person authorized to issue and redeem (permanently retire from circulation) the new units of CVC.” The guidance notes that the money transmitter definition applies regardless of whether a system “migrates” from a centralized to a decentralized system at any point in time.

ICO Sales through Derivatives. The second type of ICO business model addressed by the guidance involves an ICO that raises funds “by selling an equity stake or a debt instrument to early backers, or hedges a previous investment in CVC through a derivative, such as a futures contract.” In these instances, the guidance notes that “investors receive a digital token as proof of investment.” The guidance notes that application of the BSA will vary in these situations based on the whether the investors ultimately receive a new CVC, receive a DApp coin, use the original token as a new CVC or DApp coin, or receive some other type of return.

ICO Exemptions. The guidance notes that certain ICO issuers are exempt from the definition of an MSB. These include “a bank, foreign bank, or a person registered with, and functionally regulated or examined by the SEC or CFTC.” The guidance also indicates that ICO issuers may qualify for the MSB exemption that applies “when the acceptance and transmission of value is only integral to the sale of goods or services different from money transmission,” and states that this exemption generally applies “unless the asset is issued to serve as value that substitutes for currency.”

Purchase and Resale of ICO Tokens. The guidance indicates that ICO investors who resell tokens generally do not have BSA obligations, unless the investor is engaged in activities that trigger BSA obligations related to a broker-dealer in securities, futures commission merchant, introducing broker in commodities, or other related regulatory frameworks.

DApps Financed by ICOs. The guidance indicates that DApps financed through ICO fundraising are subject to the same obligations as other DApps. Accordingly, DApps that accept and transmit value are money transmitters, and owners/operators of a DApp that accepts and transmits value may also be considered money transmitters. However, the guidance indicates that the actual development of the DApp “consists of the production of goods or services, and therefore is outside the definition of money transmission.”

Pre-Mined CVC. With regard to pre-mined CVC, the guidance states that “[t]o the extent that a person mines CVC and uses it solely to purchase goods or services on its own behalf, the person is not an MSB.” However, “if a person mines CVC and uses it to engage in money transmission,” the person will be deemed a money transmitter.

Mining Pools and Cloud Miners. With regard to CVC earned via mining pools or cloud mining, the guidance distinguishes between circumstances where the pool operator merely transfers CVC earned to the pool members, and circumstances where the pool operator also hosts wallets on behalf of the pool members. In the first case, the pool operator is not a money transmitter, because any money transmission is merely integral to the operator's main services coordinating the combined resources of the mining pool members. However, where the pool operator also hosts wallets for the mining pool members, the guidance indicates that the pool operator would be a money transmitter.

Available Resources

Compliance Expected Before Launch. The guidance states that “FinCEN expects that persons introducing innovative products or services to a highly regulated activity, such as money transmission, will ensure that the innovation complies with the regulatory framework applicable to such activity before the innovation is taken to market.”

Resources. The guidance points to various resources available to industry actors and includes a table with links to related FinCEN guidance.

Engaging with FinCEN. The guidance references procedures for approaching FinCEN to request individual guidance or an administrative ruling on a particular situation.

Money Transmitter Status of Certain Cryptocurrency Business Activities	
P2P Exchangers	Money Transmitter, unless P2P exchange activity is infrequent and not for profit/gain.
Hosted CVC Wallets	Money Transmitter, with obligations based on status of wallet owner including Funds Travel Rule compliance.
Unhosted Wallets	Not Money Transmitter.
Multi-sig Wallets	Money Transmitter if services are combined with hosted wallet services.
CVC Kiosks (ATMs)	Money Transmitter.
DApps	Money Transmitter (including owner/operator) if DApp accepts and transmits value.
Anonymizing Services Providers (e.g., "Mixers," "Tumblers")	Money Transmitter.
Anonymizing Software Providers	Not Money Transmitter. However, persons who use may be money transmitters and may have Funds Travel Rule obligations.
Providers of Anonymity-Enhanced CVCs ("Privacy Coins")	Money Transmitter if developer/provider is engaged as a business in transmitting value in CVC. Persons who use privacy coin CVCs to accept and transmit value from one person to another person or location are Money Transmitters.
Transmitters of Anonymity-Enhanced CVCs ("Privacy Coins")	Money Transmitter. Funds Travel Rule obligations apply.
CVC Payment Processors	Money Transmitter.
Internet Casinos	May be Money Transmitter if accept and transmit value in CVC.
CVC Trading Platforms and Decentralized Exchanges	Not Money Transmitter if only provide forum where buyers/sellers settle through outside venue. Money Transmitter if purchase CVC from seller and sell to buyer.
ICO Issuers Selling to Distinct Buyers	Money Transmitter. Exceptions may apply for banks, SEC/CFTC regulated entities, and in circumstances where money transmission is "integral" to sale of other goods or services different than money transmission.
ICO Issuers Selling through Derivatives	BSA obligations will vary based on what investors ultimately receive.
DApps Financed by ICOs	Money Transmitter (including owner/operator) if DApp accepts and transmits value. Actual development of DApp is not money transmission.
Pre-mined CVC	Money Transmitter if person mines CVC and uses it to engage in money transmission.
Mining Pools and Cloud Miners	Money Transmitter if pool operator also hosts wallets for pool members.