Finalised Guidance

Approach to International Cryptoasset Firms (ACIF)

FG26/7

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1 Executive Summary

1.1 This non-Handbook guidance sets out our general approach to international cryptoasset firms providing, or seeking to provide, cryptoasset services that require authorisation in the UK. It aims to provide clarity on how we will assess international cryptoasset firms against minimum standards both when they apply for authorisation and on an ongoing basis.

1.2 Our baseline expectation is for firms requiring FCA authorisation to carry out their regulated cryptoasset activities from a UK legal entity. This is subject to some specific exceptions where we see a case for overseas cryptoasset firms serving UK customers through a UK branch to be authorised as a qualifying cryptoasset trading platform (QCATP) operator. In such cases we expect the home regulator to have comparable levels of regulatory protection and regulatory requirements in place, as determined by the FCA.

2 Glossary

Term	Definition
UK legal entity	UK individual, or partnership, body corporate or unincorporated association incorporated or formed under the law of any part of the United Kingdom
UK branch	One (or more) permanent place(s) of business which: i. is (are) in the UK ii. has (have) no legal personality of its (their) own; and iii. is (are) legally dependent on the international cryptoasset firm

3 Background and Context

3.1 The government's legislation (the Cryptoassets Regulations) determines whether a person needs to be authorised for cryptoasset activities. The threshold conditions in Schedule 6 FSMA - supplemented with FCA guidance – determine the minimum standards that need to be met for successful authorisation for these activities. Part of this is consideration of the legal structure of the applicant, including where it is incorporated or established and what this means when it comes to, for example, our ability to adequately supervise the firm. As explained in the summary chapter of PS26/13, existing, general COND guidance on interpreting the threshold conditions to cryptoasset firms will also apply.

3.2 This AICF guidance does not change existing rules for cryptoasset firms or other provisions in the FCA Handbook. It should be read in conjunction with:

- The government's Cryptoassets Regulations
- The FCA's Approach to international firms
- The FCA's policy statements and rules on cryptoasset activities

4 Our objectives and approach for considering applications of crypto firms

4.1 We are seeking a competitive and open financial system, but we also need to approach our assessment of the threshold conditions with our statutory objectives in mind.

4.2 Additionally, we have looked to provide as much clarity as possible to firms about our requirements and expectations so that they can get ready for the commencement

date set by the Cryptoassets Regulations and get authorised under Part 4A of the Financial Services and Markets Act 2000 (FSMA).

5 Who this guidance applies to

5.1 This guidance is relevant to firms that require FSMA authorisation in the UK for any of the activities in Table 1, below. This includes (i) firms who are already FSMA authorised for other, non-crypto, regulated activities (who will need a variation of permission), (ii) crypto MLR-registered firms which are not yet FSMA authorised, (iii) firms currently serving UK customers by making use of the 'section 21 gateway' who are not yet FSMA authorised, nor registered under the crypto MLR regime.

5.2 Firms that are, or will be, dual-regulated by the FCA and the PRA should also read this guidance to familiarise themselves with the FCA's general approach to assessing whether international cryptoasset firms meet our threshold conditions. However, such dual-regulated firms will not necessarily be expected to carry on the new cryptoasset activities through a UK legal entity if they can demonstrate at the FCA authorisations gateway, and on an ongoing basis, that they can meet the threshold conditions by operating from a branch. This will be assessed on a case-by-case basis by the FCA before it provides consent:

- to an authorisation, or
- to a variation of permission for dual-regulated firms to the PRA; or
- as part of supervisory engagement once authorised, to a firm that is considering restructuring.

Table 1

Activity name	**Legislation ref.**
Issuing qualifying stablecoin	Article 9M
Safeguarding of qualifying cryptoassets or relevant specified investment cryptoassets	Article 9N(1)(a)
Arranging for another person to safeguard qualifying cryptoassets or relevant specified investment cryptoassets	Article 9N(1)(b)
Operating a qualifying cryptoasset trading platform	Article 9S
Dealing in qualifying cryptoassets as principal	Article 9T
Dealing in qualifying cryptoassets as agent	Article 9W
Arranging (bringing about) deals in qualifying cryptoassets	Article 9Y(1)

Activity name	Legislation ref.
Making arrangements with a view to transactions in qualifying cryptoassets	Article 9Y(2)
Arranging qualifying cryptoasset staking	Article 9Z6

5.3 It is important to consider the Cryptoassets Regulations in the first instance, as some international crypto firms may not require authorisation in the UK, depending on the nature of their activities and customer base. Firms should consider carefully:

- The nature and scope of their activity against the definitions of the regulated activities (see Articles 9M, 9N, 9S, 9T, 9W, 9Y, 9Z6).
- The various exclusions in the Cryptoassets Regulations; for example, the "group activity" exclusion (Article 9O), the "temporary settlement arrangements" exclusion (Article 9Q), the "absence of holding out" exclusion (Article 9U) and the "introducing" exclusion (Article 9Z1), as well as other available exclusions set out in the Cryptoassets Regulations.
- The composition of their UK client base and whether their activity meets the "carrying on regulated activities in the United Kingdom" test (see amendments to section 418 of FSMA under Part 4 of the Cryptoassets Regulations).
- Whether their activity meets the "by way of business test" (see the Regulated Activities Order, and regulation 44 of the Cryptoassets Regulations).

5.4 For firms outside our regulatory perimeter, this AICF guidance does not apply (although we will have regard to an applicant's close links and connections with other persons, as per the threshold conditions).

5.5 In addition to this guidance, dual-regulated firms who are intending to carry out any of the activities in Table 1 should refer, for further information, to:

- The FCA's Approach to international firms.
- Any rules or guidance from the Bank of England on systemically important payment systems that use digital settlement assets (DSA), such as stablecoins, and DSA service providers.
- The PRA's Approach to international firms.

6 Assessment of threshold conditions and key considerations

6.1 The threshold conditions for authorised persons (who are not PRA authorised persons) are as follows:

Table 2

Threshold condition	Legislation ref.	FCA guidance ref.
Location of Offices	FSMA Schedule 6 Para 2B	COND 2.2

Threshold condition	Legislation ref.	FCA guidance ref.
Effective Supervision	FSMA Schedule 6 Para 2C	COND 2.3
Appropriate Resources	FSMA Schedule 6 Para 2D	COND 2.4
Suitability	FSMA Schedule 6 Para 2E	COND 2.5
Business Model	FSMA Schedule 6 Para 2F	COND 2.7

6.2 We have set out below a consideration of these, including some examples of the risks of harm we are most concerned to mitigate for international crypto firms.

Location of Offices

6.3 The location of offices threshold condition creates requirements for firms which are incorporated in the UK and/or have head offices in the UK. Since this is not directly relevant to overseas firms, we have not considered this further here.

Effective Supervision

6.4 Firms must be capable of being effectively supervised by the FCA at all times. In simple terms, the FCA needs to be able to monitor and oversee a firm's activities without obstructions. We pay close attention to the way in which the firm's business is organised, taking into account group structures, close links, and arrangements with third parties.

6.5 The FCA recognises the highly digital, mobile and cross-border nature of the crypto industry; that crypto firms may have existing headquarters overseas as well as relatively geographically dispersed profiles of infrastructure, employees and key decision makers. However, as with all international firms, it is important for us to ensure that an appropriate amount of a crypto firm's control function activity, leadership and decision-making ("mind and management") is in the UK. Taking stablecoin issuance, for example, we anticipate that qualifying stablecoins will be used as money-like instruments within the UK and internationally. This will require effective supervision to ensure oversight of controls and the ability to intervene when necessary to address harms quickly. Another key element of effective supervision is the ability to have efficient access to information about a firm's business, products, customers and activities as well as the ability to intervene to prevent or mitigate risks of harm.

6.6 Cryptoasset regulatory frameworks are evolving and being implemented at different scales and paces across different jurisdictions. In some jurisdictions, comprehensive supervisory cooperation arrangements between regulators have not yet been developed. This heightens the risk that, where firms do not provide direct access to relevant supervisory information or otherwise do not act in accordance with our expectations, we are unable to secure effective outcomes and address harms in line with our objectives. We will assess potential mitigants proposed by firms for these increased risks of harm to consumers or markets.

6.7 In line with the Approach to international firms, we will pay close attention to the supervisory cooperation with the firm's home state regulator. It is important to be able to share information, and to rely on the home state regulator to take action, where we might not be able to because of geographical or legal constraints. The way

in which crypto firms are organised also requires scrutiny, noting the challenges which can arise from extensive and complex group structures, close links, and outsourcing arrangements of some international firms.

Appropriate Resources

6.8 The appropriate resources condition exists to ensure that firms have sufficient financial resources – including capital and liquidity buffers - to meet their ongoing obligations and withstand stress events.

6.9 We are particularly concerned about the risk of harm if an international firm safeguarding client cryptoassets fails. It is more likely that an overseas firm (including one operating with a UK branch) is subject to the insolvency regime and procedures of the firm's home state, which may not provide the same protections as Client Assets Sourcebook (CASS) rules and UK insolvency law, and which the FCA may have limited ability to effectively participate in or influence. Insolvency regimes across different jurisdictions can vary considerably and there is little harmonisation of insolvency law at an international level, and in particular regarding cryptoassets. An insolvency practitioner appointed in the home state may not, therefore, be in a position to observe UK protections when distributing cryptoassets.

6.10 As a result, the protections offered by the applicable provisions of CASS, in conjunction with UK property and insolvency law, might not be applied if the insolvency is administered in line with the home state's laws, might only be partially applied, or might be applied only if certain conditions are met.

6.11 Client cryptoassets may not be ring-fenced as CASS and UK law had intended. This could be an issue if, for example, the client cryptoassets are made available to the international firm's general creditors as part of the general insolvency estate of the firm, and clients for whom cryptoassets were safeguarded under CASS have to prove their claims as creditors rather than beneficiaries to property.

6.12 This risk of harm is amplified by:

- Legal uncertainty: there is limited clarity and consistency on property and ownership rights for cryptoassets (and a lack of relevant case law and precedent) as legal frameworks across jurisdictions are being revised and clarified. Foreign courts may develop a different basis to determine clients' ownership rights, which may negatively impact outcomes in insolvency for UK consumers.
- Cryptoassets are safeguarded and settled in fundamentally different ways to traditional assets, and safeguarding technologies are still evolving and maturing.

6.13 The appropriate resources condition also requires us to consider whether there are adequate non-financial resources such as staff and experienced senior managers. Our Approach to international firms clarifies that we typically expect senior managers who are directly involved in the firm's UK activities to spend an adequate and proportionate amount of time in the UK. This expectation will apply equally to cryptoasset firms, notwithstanding the digital and mobile nature of many crypto businesses.

Suitability

6.14 The suitability condition focuses on whether the firm is fit and proper, with competent leadership, prudent risk management, and behaviour which is in line with good practices and standards.

6.15 Relevant considerations such as competence, capability, integrity – are a function of the firm's key personnel and risk management frameworks and should be considered case-by-case. We generally do not see reason for structural or systematic differences between crypto and traditional regulated financial activities.

Business model

6.16 The Business Model condition requires the FCA to think carefully about how a firm's business works, and whether it is sustainable and well-controlled. Firms should operate in a sound and prudent manner, protect consumers, and uphold the integrity of the UK financial system.

6.17 Again, we do not see any reason for significant structural or systematic differences between crypto and traditional regulated financial activities. However, we have previously pointed towards deficiencies in business plans as a common reason for unsuccessful MLR registration applications by crypto firms.

6.18 Cryptoasset activities are characterised by a high degree of direct retail participation. UK stablecoin issuers will also be required to provide redemption to all tokenholders, the majority of whom are likely to be retail customers in the UK.

7 What this means for future regulated cryptoasset firms

7.1 Potential harms to consumers and markets could be more likely to occur where regulated activities are undertaken by international firms from UK branches or overseas offices rather than through UK legal entities. It is more challenging for the FCA to monitor current and emerging risks, obtain timely and accurate information from firms or third parties, and to intervene to require firms to take or refrain from certain actions. Furthermore, customers – especially retail consumers – may be unclear on these higher risks of harm when engaging with an international firm versus a UK crypto firm. Our recent consumer research shows that consumer misunderstandings of cryptoasset risks remain high and in some cases are rising (for example, in relation to compensation if they experience losses).

7.2 For cryptoasset activity some of the risks of harm are more acute. This is in part because it may be more complex for us to take certain actions in relation to international firms, such as successfully participating in insolvency proceedings or requesting and obtaining information in the absence of well-developed domestic and cross-border legal and regulatory frameworks.

7.3 In all cases, therefore, we expect firms seeking FCA authorisation for cryptoasset activities (Table 1) to have a presence in the UK. This is aligned to our position in the Approach to international firms. We cannot adequately supervise the conduct of a firm's UK business without this.

7.4 Further, our baseline expectation is for firms requiring FCA authorisation to carry out their regulated cryptoasset activities (Table 1) from a UK legal entity. Generally, we do not expect a UK branch alone to be compatible with our minimum standards or to mitigate risks of harm, especially for client assets upon firm failure, and supervisory cooperation.

7.5 However, we have outlined some exceptions to this position regarding a UK legal entity below.

7.6 Notwithstanding the expectations set out above, all individual applications will still need to be considered on their merits and on a case-by-case basis, considering all relevant factors.

8 Exceptions

Operating a Qualifying Cryptoasset Trading Platform (article 9S)

8.1 In line with DP25/1 and CP25/40, we see a case for the activity of operating a QCATP to be carried out through a UK branch where this can facilitate access to global liquidity in order to achieve better price and execution outcomes for clients. Where possible, we want to avoid restrictions or frictions – whether created by legal entity fragmentation or other reasons – which prevent UK orders from being able to be matched with overseas orders.

8.2 A QCATP is a marketplace where multiple third party buy and sell orders interact. This is different, for example, from a principal dealer model where the dealer acts as the counterparty to the buyer or seller. The multilateral nature of trading on a QCATP, together with a UK QCATP's admission requirements and unique role in the functioning of the market abuse regime, point, in our view, towards a differentiated approach to authorisation of their operators. This is further supported, in some cases, by the advantage of access to global liquidity in enabling a QCATP's more effective functioning and better service to its users.

8.3 This may give international firms, depending on their business model, more flexibility to deliver better execution outcomes for UK customers.

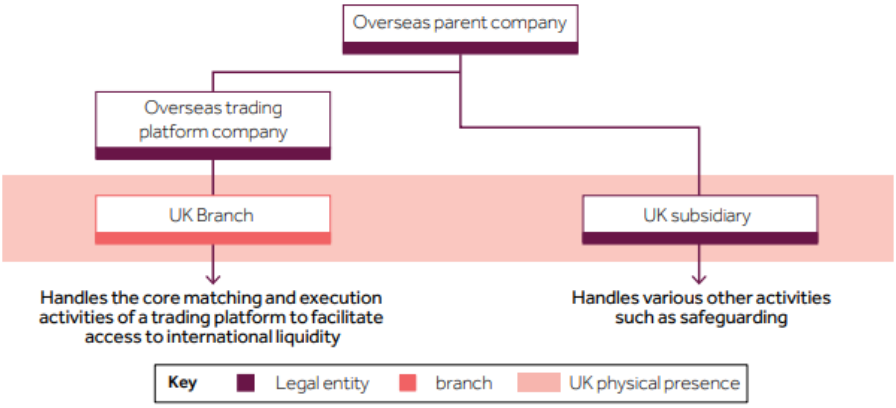
8.4 Where a firm applies for authorisation to operate a QCATP in the UK via a branch, it should explain in its application - and, where relevant, during supervisory communications for any structural changes following authorisation - why this structure is appropriate for its business model. We do not expect all UK QCATP operators to carry out this activity through a branch but rather those that can offer access to global liquidity pools where this may enable better outcomes for UK customers.

8.5 Where a firm seeks authorisation, the FCA will authorise the whole firm, including its UK and overseas offices. For an overseas firm making use of a UK branch to be authorised, we expect the home regulator to have comparable levels of regulatory protection and regulatory requirements in place, as determined by the FCA. We would not consider a letter of good standing on its own to be sufficient.

8.6 Figure 1 shows one potential example of a legal entity structure we believe could be compatible with our regulatory target outcomes. In the example in Figure 1, an international crypto firm would have both a UK branch and a UK legal entity. The UK branch would handle functions which are central to a UK QCATP's operation, enabling UK investors' orders to interact with orders of overseas investors. This is one way in which UK investors would have access to superior price and execution outcomes than if they were restricted to isolated liquidity pools.

8.7 The UK legal entity could handle other regulated activities like safeguarding. Individual UK QCATP applications will still need to be considered on their merits and on a case-by-case basis, considering all relevant factors including the needs of and risks to consumers.

Figure 1 – CATP serving UK customers through branch model



Restricted principal dealer permission for UK QCATP matched principal trading (restricted 9T) in a model relying on the exception above

8.8 Our rules in CRYPTO 6 permit a firm that is authorised to operate a QCATP (a UK QCATP operator) to also provide matched principal trading (MPT) services provided it obtains a principal dealer permission. However, given our general expectation that principal dealers should have a UK legal entity presence to meet our threshold conditions, a UK QCATP operator authorised via a UK branch (as illustrated above, a 'branch-authorised UK QCATP operator') would be unlikely to benefit from this MPT option. It would either need to apply for the principal dealer permission via its affiliated UK legal entity – or set up a second UK legal entity to do so, instead of (or in addition to) establishing a UK branch.

8.9 We believe this would be a poor outcome in cases where the branch-authorised UK QCATP operator is seeking to use the principal dealer permission only to provide matched principal dealing services on its own platform because:

- Legally separating the matched principal dealing service from the platform to which it relates risks creating friction that could undermine the value of that service. It may also be disproportionate given the more limited risks of the matched principal dealing service.
- In addition, setting up a second legal entity would undermine the benefits of the 'sub + branch' model we intend to be available to overseas QCATP operators seeking UK authorisation.

8.10 Therefore, overseas firms that:

i. are branch-authorised UK QCATP operators, and

ii. seek a restricted principal dealer permission to be used only for facilitating matched principal dealing on the firm's own platform

should in principle be able to obtain that restricted matched principal dealer permission based on their UK branch presence, provided they meet the other threshold conditions. (Such firms would also have to meet certain other conditions to carry out matched principal trading, such as those set out in the Handbook glossary definition and CRYPTO 6).

8.11 For the avoidance of doubt, where an overseas firm meets condition (i), above, but seeks a principal dealer permission to carry out proprietary trading (or any other trading that does not meet the matched principal trading conditions set out in the Handbook glossary definition and CRYPTO 6), the general expectation that principal dealers should have a UK legal entity continues to apply.

Restricted safeguarding permission to facilitate UK QCATP settlement (restricted 9N)

8.12 Certain QCATP operators rely on the operation of a 'float' to achieve efficient settlement of trades executed on the QCATP. This settlement float consists of a percentage of clients' and potentially the firm's assets held in a settlement wallet controlled by the QCATP operator.

8.13 In line with the geographic scope of safeguarding set out in FSMA s418 (as amended by the Cryptoassets Regulations), and under Article 9N, the entity that uses such a settlement float must have the safeguarding permission. To ensure proportionality, the safeguarding permission for this entity could be restricted, with fewer rules applying, subject to certain conditions (please see PS26/11 for more details). In particular, cryptoassets in this settlement wallet would not be held under trust and so would not be afforded the same protections from CASS rules.

8.14 Further, analogous to the exception for MPT above, a branch-authorised UK QCATP operator seeking a restricted safeguarding permission to operate a settlement wallet (and meeting the associated conditions) would not, in principle, be expected to carry out the operation of this settlement wallet from a UK legal entity to meet the threshold conditions.

8.15 However, in all other cases, the general expectation that safeguarding firms should operate from a UK subsidiary would continue to apply.

9 Next Steps

9.1 This guidance does not preclude or prejudge any recognition or deference arrangements which may be legislated for by the government in the future.

9.2 We intend to review our guidance periodically as cryptoassets legal and regulatory frameworks and supervisory cooperation arrangements mature.