

Virtual Asset Service Providers Framework Industry Consultation Response



Ministry of Finance, National Planning and Trade

And



7th March 2024

INDUSTRY CONSULTATION RESPONSE

Introduction

In July 2022, the Seychelles published its first overall national risk assessment (ONRA) assessing the money laundering and terrorist financing risks (ML/TF risks) associated with virtual assets (VAs) and virtual asset service providers (VASP). The results of that assessment determined that the Seychelles' risk exposure to the misuse of these products and services was very high. One of the main vulnerabilities identified in the ONRA relating to this finding, was the absence of a formal regulatory framework which would be applicable to this sector.

In August 2023, the Technical Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT) Committee AML/CFT Committee (TAC), under the oversight of the National AML/CFT Committee (NAC), initiated several different workstreams designed to address the various vulnerabilities identified in the ONRA, to mitigate the ML/TF risks posed by the misuse of VA and VASPs for criminal purposes.

On 19th December 2023, the NAC approved the launch of a formal consultation process, proposing the introduction of a regulatory framework that would apply to VA promoters and VASPs operating in or from the Seychelles. This consultation was formally launched by the National Anti-Money Laundering and Countering the Financing of Terrorism Committee (NAC) on 20th December 2023.

Overview of Proposed Regulatory Framework

The main objectives of the proposed framework are to:

1. Protect the Seychelles' financial stability and integrity,
2. Enable consumers to make well-informed decisions, with a clear understanding of the risks involved, and
3. Encourage growth, innovation, and competition in the Seychelles.

The Financial Services Authority (FSA/Authority) with the support of the Government and relevant stakeholders has proposed a staged approach, whereby the significant measures be adopted in a way that will ensure the greatest vulnerabilities identified in the ONRA are addressed as priority. This involves the introduction of a new regulatory framework requiring that VASPs be licensed and authorised based on activities being conducted, with VA Promoters needing to either be, a licensee under the proposed law, which shall be known as the Virtual Asset Service Providers Act (VASP Act) or appropriately licensed under the Securities Act, 2007. Initial Coin Offerings or Non Fungible Tokens will be required to be registered under the new legislation.

The second important measure was the introduction of amendments to the existing Anti-Money Laundering and Countering the Financing of Terrorism Act (AML/CFT Act) and its Regulations, so as to ensure that VA promoters and VASPs apply appropriate controls to detect and prevent money laundering and terrorist financing risks.

Additional consequential amendments to the International Business Companies Act (IBC Act), Companies Act, the Financial Consumer Protection Act (FCPA) and legislation designed to support enforcement related activities are also being proposed.

The proposals covered by the consultation represent an important next step in a longer process, with further work anticipated as the sector continues to evolve and authorities gather further information on the industry. This will form part of a longer-term action plan, to be overseen by the NAC.

Summary of Consultation Responses

An appreciation is extended to all participants and stakeholders for the large number of responses received. These were both welcome and appreciated. Particular aspects of the consultation document attracted more feedback than others. The Authority has taken careful note of all responses even if opposing views were, at times, difficult to reconcile. Due to the diversity of responses received, in formulating its adopted position, the Authority has sought to primarily remain faithful to the general objectives put forward in the consultation document, as summarised above.

The overall goal of the work undertaken to date, is to update, upgrade and converge the requirements of the current financial services framework to establish a more consistent, coordinated, robust and proportionate risk-based approach while protecting the integrity and improving the governance of this sector. The Authority is mindful that some of the proposed changes will not take place overnight. As was emphasised during the consultation, this is the start of the Seychelles journey, with further changes to be made in the future, on a risk-basis. Efforts will be made to ensure that further consultation on future possible changes takes place, allowing stakeholders sufficient time to align themselves to the new requirements.

Response to the Consultation

The Authority launched the public consultation on 20th December 2023, inviting both written responses and attendance at a hybrid virtual and in person live consultation session, which took place on 9th January 2024.

In total approximately 15 detailed written responses have been received, and approximately 50-60 participants attended the live consultation process. Owing to the impact the proposed regulatory framework may have on specific sectors, the Authority also held dedicated discussion sessions with members licenced under the Securities Act, members of the International Corporate Service Provider sector and representatives from VASPs currently operating in or from the Seychelles. In addition to private sector participation, feedback was also sought from authorities and agencies represented on the TAC.

The Authority would like to thank all participants for investing the time and providing their professional insights concerning propose regulatory frame work.

Consultation Outcomes

The FSA has carefully considered the responses received during the consultation. It has also shared and discussed these responses and the proposed way forward with the agencies and authorities represented on the TAC and the NAC. The following section summarises the insights received, and responses provided, the feedback has been grouped by key topic/areas.

Adoption of licencing authorization framework

Overall, there was agreement across all stakeholders for the adoption of a licencing framework.

One participant queried whether it would be possible to receive a licence in principle, allowing VASPs time, following the transition period, to put in place the necessary controls as would be required by the VASP Act, once in force. The FSA is mindful that the financial crime risk exposure assessed in the ONRA as very high, requires that controls to mitigate ML/TF risk be in place as of the time of authorisation, to reduce any risk that VASPs or VA services are misused by illicit actors. Reliance upon a “license in principle” approach, would provide the Seychelles with assurance that VASPs have invested in appropriate controls to mitigate these risks, from the moment they are authorised. This approach however, does not provide applicants with certainty around their authorisation status, as this

merely prolongs a final determination regarding their official licensed status, to an indeterminate date in the future.

The FSA is mindful that applicants will need to invest adequate time to properly prepare and submit information. There are other requirements, such as those relating to substance and capital requirements, which may also take time for applicants to organise in order to meet same. To ensure there is sufficient time for applicants to make these arrangements, it is proposed that the proposed VASP Act include a transition period of which would last, until 31st December 2024. This period is afforded only to VASPs currently operating in and from the Seychelles to submit a completed licence application. Parties conducting VASP activities, as will be defined in the VASP Act, after 31 December 2024, will be considered to be undertaking unauthorised activity, and will be dealt with accordingly. Any new VASP (created on or after the date of coming into force of the VASP Act) will have to submit an application and obtain the relevant licence before it can undertake any virtual asset services. Hence, the transitional period.

However, attention must be drawn to the AML/CFT Act amendments which will capture entities operating VASP services as reporting entities which will then render the AML/CFT Act applicable. Existing operators will be subject to enhanced supervision, during the transitional period, with an emphasis on AML/CFT.

This transition period will also facilitate the Authority's resourcing and capacity, to ensure that applications can be properly reviewed and dialogue with applicants conducted, on a risk-basis, with sufficient time and resourcing.

Definition of VASP Activities

Participants noted that there were several terms that required defining and clarification. One of these, was the scope of VASP activities that would require authorisation. Both the definitions and the authorisation scope have been updated in the draft bill to clarify specific terms and target activities.

Registration of ICOs/NFTs

No material concerns were raised about the proposed registration regime in relation to the promotion of VAs or Initial Coin Offerings or Non-Fungible Token (NFT) in or from the Seychelles. Clarification was recommended concerning the definition of these terms, and to ensure that regulatory requirements clarified the process that must be followed for registration.

One important consideration raised concerns as to the types of applicants who would be able to apply to register such promotional schemes. The ONRA disclosed that one of the financial crime risks to which the Seychelles is exposed, relates to receiving proceeds obtained through the mis-selling of VAs. Globally, some of these illicit schemes have been promoted by individuals and organisations, who are not fit and proper or not required to be authorised, meet governance and AML/ CFT standards. In some cases, these illicit schemes originate outside of the Seychelles, making it difficult for authorities to intervene in order to disrupt their activities.

In order to mitigate these risks, there will be a limit as to who will be deemed eligible applicants for the purpose of applying for registration. This will either be an entity licensed as a VASP under the proposed VASP Act or authorised entities licenced under the Securities Act. Parties located outside of the Seychelles will not be eligible to register VA or NFT promotion schemes.

One participant asked whether a VASP operating an exchange platform would be required to ensure that promoters of VA or NFTs on its platform were appropriately registered. The Authority reviewed the registration requirements and noted there was a risk that promoters who attempt to register VA or ICO products, may be located outside of the Seychelles, and therefore not being subject to equivalent AML/ CFT requirements or market abuse prevention requirements.

The Authority would have little or no authority by which to take relevant action against such promoters who engage in this type of activity, with an emphasis on the mis-selling of such products, especially if aimed or targeted at Seychelles consumers. The ONRA disclosed that the Seychelles was vulnerable to promotions of this nature, wherefor false claims of affiliation and links to the Seychelles, via VASP exchanges being the prominent determining factor. In order to mitigate this risk, the Authority is proposing that promotion of VA or NFTs in or from the Seychelles must not only be registered, but that only an appropriately licenced VASP or authorised entities under the Securities Act will be authorised to apply for such registration.

The aim is to ensure that the promotion of any VA or NFT products, are not undertaken in a misleading manner, or vulnerable to market abuse. The Authority acknowledges the risks associated with an authorised VASP creating and supporting its own token product as being different from an external third-party product which may be promoted to consumers or other parties. The Authority would expect that authorised VASPs who promote new VA or NFT post-authorisation, should have in place controls which verify the provenance of its development, terms of its promotion and assess the associated risks before listing such products. The Authority will seek to engage further with VASP representatives taking part in the Working Group to ensure that these requirements are fit for purpose and address the risks sought to be mitigated.

Clarification was requested during the consultation as regards to the promotion of VAs, where it has been developed by the VASP itself, and the criteria for registration. The Authority will ensure that supporting regulations are developed, closely reflecting the requirements of the Mutual Fund and Hedge Fund Act for the promotion and registration of such schemes. Further clarification will also be provided about the types of VA or NFTs that may be exempt from registration, on a risk basis, to ensure these do not unintentionally expose the Seychelles to unmitigated financial crime risks. Such exemptions will be assessed, focusing the inherent nature or use of the VA or NFT, as opposed to a particular named offering.

Primary Licence Legislation

Omissions in terms of definitions and processes were highlighted, for which the FSA has undertaken the necessary steps to ensure that they are addressed, whether within the primary act itself or on any of the supplementary legislative tools.

Lead Supervisor

No comments were provided on the proposal that the Financial Services Authority be designated as the lead supervisor for VASPs.

Concerns were raised as to resourcing capabilities and whether the Authority will have the necessary capacity to maintain industry service standards. The necessary steps have commenced to ensure that consideration is had in the budget to reflect the requirements both in terms of personnel and technology. The Authority will leverage existing resources, with experience and knowledge as to the internal processes for authorisation and supervision. During the ongoing works to put into place this regulatory framework, staff have undertaken relevant training with the intention of continuing ongoing education.

The FSA has commenced work to determine the type of technology and software necessary to ensure effective measures are in place. The FSA will proceed with a gap analysis to ensure that any engagement is one which is beneficial and useful.

A financial institution, as defined under the Financial Institutions Act 2004 may, with the written approval of the Central Bank, apply for a licence to carry out the business activities of a virtual asset service provider through a subsidiary. The holder of a payment service provider licence issued under the National Payment Systems Act, 2014 may, with the written approval of the Central Bank, apply,

through a subsidiary, for a licence to carry out the business activities of a virtual asset service provider. At this time, no indication was received of any such licensees intending on applying for such authorisation. Going forward, the Authority and the Central Bank will continue their close engagement to ensure that the criteria applied for such approval and subsequent authorisation is commensurate with the jurisdictions VA and VASP risk appetite.

Authorisation Approach

Suggestions were made as to the possibility of the FSA adopting an ‘approval in principle’ approach to licensing. Questions as to whether the Authority had capacity to be able to receive, process and approve applications within a reasonable timeframe, were posed.

The Authority remains dedicated to maintaining service standards that are efficient whilst ensuring that ‘bad actors’ are not given legitimate access to the field of play. Approvals in principle have been ill used in the past, and the drawbacks of the same far outweigh the benefits. Where existing licensees are concerned, the FSA will allow continued operations until the 31st December 2024 provided that a complete application is lodged. Once the transitional period has lapsed, any persons found to be operating VA or VASP activities falling within the scope of the enacted VASP Act, will be in contravention of the law and therefore subject to the appropriate sanctions and punitive measures. The Authority aims to ensure that players within the space are authorised to be doing so.

Eligible Applicants

Matters surrounding who may submit an application were an area of interest. This differs in relation to who is eligible to be an applicant (i.e. a domestic company or an IBC) but rather focuses on who can essentially ‘push’ or apply for authorisation on behalf of another party.

The general proposal was to allow for licensees under the ICSP Act, namely the Corporate Service Providers (CSPs), to submit applications on their clients’ behalf. The FSA has yet to make a final decision on whether this will be the way forward. Consideration must be had as to whether the current licenced CSPs have, at this time, sufficient expertise and knowledge of VA and VASP operational activities, including the complexities of the products they may support, compliance, technology and cybersecurity requirements, not to mention the potential risk appetite for taking on the legal responsibilities of ensuring that all information contained in applications are true and accurate, as the onus will be on them to ensure same.

Further discussion will be undertaken with this sector to better gauge whether this would be feasible in practice. In the interim, the FSA will not be allowing a CSP to act as an agent, on or on behalf of a VASP, for the purpose of submitting applications for authorisation under the proposed VASP Act. Whilst a CSP may be engaged to assist in completing the same, responsibility for the completeness and accuracy of the information submitted will remain and rest solely on the VASP itself. This will also include answering any questions the FSA may have during the licensing process.

Authorised Activities – Scope

Overall, participants did not raise any objections to the category of activities for which authorization would be required under the draft bill. The Authority is aware of that, in order to facilitate the authorization process, further details are needed to explain the types of investment- related activities which would fall under the scope of authorised activities. This is especially important for Securities Dealers operating in and from the Seychelles. The definition of authorised activities will therefore be elaborated upon to identify the following activities for which authorization will be required:

- custody and administration services,
- the operation of a trading platform in respect of crypto-assets,

- the exchange of crypto-assets for funds/crypto-assets for other crypto-assets,
- the execution of orders on behalf of third parties,
- placement services,
- transferring crypto-assets from one address or account to another address or account,
- the reception and transmission of orders,
- investment advice, and
- portfolio management services.

Attendees sought clarification around the activities which would be permissible under the proposed framework, whether considerations could be had to remove activities such as non-custodial services, activities based DeFi, Web3, whether the framework captured unhosted wallets and classification of VA and coins. Clarification was also sought as to whether the Authority will be requiring that persons developing or generating programs or tools which could be used by potential VASPs to support or delivery their activities would be permitted under the proposed VASP Act.

Non-Custodial Services

With regard to non-custodial services, the FSA has taken note that the FATF presently does not require the regulation of the same. The draft bill will be amended to remove these services from the current licensable activities. However, this does not remove the obligations imposed upon a VASP should they opt to make use of such services. The onus will be on a licensee to ensure that they have the appropriate safeguards in place, so as to not negatively impact or affect the regulated aspects of their business. The Authority will continue to monitor this space, and assess the potential and actual risks which may be imported onto the jurisdiction, and may opt to revise its position at a later date.

Web3

The proposed legislation aims to regulate activities undertaken by the VASP themselves. Software development or other similar activities are already regulated and falls within the category of creation of a ‘tool’ and not necessary a VA-related service, despite it being able to be used by VASP. This approach is in line with international norms.

Categories of VA/coins

In furtherance of the above, questions were raised as to whether the draft bill was intended to place restrictions on the types of coins/ assets that will be allowed. The proposal made was for the FSA to generate an acceptable list. Whilst the term “VA” is defined in the bill, the FSA will issue additional guidance for clarity about coins themselves. Guidance will provide for the nature and characteristics of the coins/ VA rather than naming them outright e.g. monero. With the ease of creating a new form of VA, the list itself would be forever changing, however, the nature, characteristic and purpose of a coin would remain relatively similar. The FSA aims to especially preclude assets whose main characteristic and purpose is subjugation.

Decentralised Finance (DeFi)

Participants asked whether the scope of the draft bill, extended to requiring authorization in order to undertake DeFi services or promote DeFi products. The Authority is currently reviewing the extent of the jurisdiction's potential exposure to DeFi-related activity and products. Some jurisdictions have opted to require that partially decentralised crypto services must apply for authorization, while those which are fully decentralised without any intermediaries are excluded from scope. The question of control and the extent to which such services are overseen by a formalised governance structure, is also an important consideration.

The Authority will have regard to the final report with policy recommendations for DeFi as published by the IOSCO in December 2023¹, in deciding the appropriate treatment of these products and services. This report acknowledges how illicit activity such as cyber exploits and attacks exploit the vulnerabilities associated with these products and services, resulting in losses for investors and other DeFi participants. Additional reports describe the risk of DeFi protocols being used as a means to convert stolen cryptocurrency from one type to another that is more liquid or less volatile, along a payment chain and finally converted into fiat currencies at a centralised VASP.

The Authority will therefore publish by way of regulations and guidance, the criteria based upon which a DeFi product or service will require authorization under the proposed VASP Act by adopting an approach which ensures that the possible misuse of these to facilitate financial crime can be appropriately and effectively mitigated.

Ineligible Applicants and other Prohibited activities

No contentious comments were received as to the prohibition of individuals from applying for a licence. This was generally accepted and will be maintained.

However, questions were raised in regards to prohibited activities, namely mining, mixers/ tumblers and validators. This centred mainly, not on whether the authority will consider including same as licensable activities but rather if this will extend to a prohibition of licencees partaking in the use of such tools and/ or services.

The FSA maintains its position, that it will not be categorising the above list as being a permissible offering made under a VASP licence; however, in the event that a VASP opts to partake in such services, the obligation will reside with the licensee to ensure that they are capable of offering such services in a safe and regulated manner, without running the risk of impacting the licensee's ability to operate within the confines of the laws of Seychelles. Definitions concerning these types of ineligible activities will be added to the draft bill. The Authority will monitor the use of these services by authorised VASPs, to verify that the potential ML/TF risks associated with their use are being appropriately and effectively detected and mitigated.

Comments were received concerning the restrictions regarding payment processing. The intent behind this prohibition, is based on conducting "payment services", as defined under the National Payment Systems Act (NPSA). As explained in the policy paper, any undertaking relating to payment services for the conduct and offering of virtual asset services using virtual asset shall be prohibited. The following activities are considered as payment services:

- (a) services enabling deposits and withdrawals,
- (b) execution of payment transactions,
- (c) issuing and or acquisition of payment instruments,
- (d) Money remittances and
- (e) Services functional to the transfer of money.

The restrictions on services listed in (a) – (e) do not extend to the following activities as defined within Appendix 3 of the VASP policy paper:

- Virtual asset wallet providers
- Virtual asset exchanges
- Virtual asset broking
- Virtual asset investment providers

¹ See: [IOSCOPD754.pdf](#). Available at: <https://www.iosco.org/library/pubdocs/>

No business is permitted to offer payment services instruments in virtual assets such as the provision of debit and credit cards, ATM kiosks, cheques and point of sale terminals.

Licensing Criteria

In general, participants did not raise any concerns about the authorization requirements, however, there were questions raised concerning Capital Adequacy and Solvency requirements and Cyber Security.

Capital Adequacy and Solvency requirements

In respect to capital adequacy and solvency requirement, the main question concerned the minimum amount of capital that would need to be evidenced. The Authority is mindful of cases in other jurisdictions where VASPs, and in particular exchanges, have collapsed or been unable to satisfy or meet their creditor obligations. The Authority is also mindful that sufficient capital should be invested to demonstrate the applicant's ability to invest in appropriate technology and internal controls to ensure that both operational and financial crime risks are effectively managed and mitigated.

The chosen way forward is to indicate the Capital Adequacy and solvency requirements within the accompanying regulations. This will make reference as to what must be maintained for each permissible activity, as well as the manner in which it is to be applied. Namely, in the event that VASP undertakes more than a single activity, they will have to make the appropriate allocations, to meet each the respective prescribed capital requirements².

However, prior to the issuance of the regulations, the FSA will be undertaking a jurisdictional comparative analysis, as well as undertake an industry wide consultation prior to implementation.

CyberSecurity

In respect to CyberSecurity, participants found that the proposed quarterly requirement for penetration testing would be overly onerous and unnecessary. The Authority acknowledges the challenge this would present for some VASPs, relative to the benefit gained so as to ensure that risks of cyber attacks or hacking were being effectively mitigated. Following discussion, the recommended way forward will require bi-annual penetration testing in the first year of licencing; with an annual requirement in subsequent years. The aim is to ensure that licensees have the necessary safeguards are in place from the outset, with any remedial work being undertaken expeditiously rather than allowing ill practices to fester. This alternative proposal was received well by VASP participants, with general understanding as to the Authority's rationale.

In addition, further guidance was requested in terms of the specific IT requirements applicants would be expected to satisfy. Consideration will be had as to the type of block chain analytic tools, transactional bridges to be used for KYC and CDD purposes as well as the e-identification verification software; to be issuable by way of regulations.

Fitness and Propriety (FAP)

Overall, participants had no objections to applying the FAP framework as currently applied to other regulated entities in the Seychelles, save that specific requirements related to expertise and knowledge will need to be evidenced. This will also be applicable, again as is the case for other regulated entities, to VASP Compliance Officers.

² Treatment of Capital Adequacy requirements for existing Securities Act licensees is further addressed under the heading **Treatment for Licensees under Securities Act.**

Participants from the CSP sector queried whether services such as the provision of a professional director or Compliance Officer, would also need to meet these requirements. The Authority is mindful that the control and direction of a VASP requires that those who embody these roles must have sufficient knowledge regarding its business model and operational activities, so as to undertake effective governance and oversight. CSPs that seek to assume these roles will need to demonstrate how these requirements will be satisfied. This will also include consideration as to the individual's overall capacity to fulfil the role, relative to other obligations they may have. The Authority will reserve its right, on a risk basis, to interview individuals to verify that they will meet the VASP FAP requirements.

Fees

Feedback was received from some participants in that the proposed base fee was somewhat high compared to other jurisdictions, The Authority is mindful that it seeks to achieve a balance between fee rates that are competitive but also reflect the level of supervision required. The Authority has determined that the base fee should be set at USD 5,000.

Further clarity was sought as to the manner in which the licensing fee will be payable, namely in that there will be the base fee of USD 5,000 and the additional fee associated with the relevant activity. As such, if an entity wishes to undertake all activities, then the base fee and all associated fees in relation to each activity must be settled in order for a licence to be issuable.

Recommendations were made for the Authority to conduct a comparative analysis of other jurisdictions with a licencing regime to determine a fair but competitive rate. The Authority notes that such a comparison was undertaken and published in the policy paper. The Authority has concluded, based on this analysis that the proposed licencing fee framework is both fair and reasonable.

One participant asked whether the licence fee would be payable after a license authorisation had been granted. The Authority can confirm that as a condition of receiving the authorization, the licence fee, which entails both the base fee and relevant fee per permissible activity, must be settled as a condition of receiving the formal authorisation taking place. Further details regarding the payment of fees will be prescribed in regulations.

Refusal or Rejection of Applications

Participants raised no concerns as to the provisions in the draft bill concerning the refusal or rejection of an authorization application. The Authority is mindful of comparative experience of other jurisdictions in relation to the quality of applications submitted. The nature of information required to determine whether a licence should be granted, can be extensive, complex and require careful review and consideration. Applicants are expected to ensure that materials submitted are complete and satisfy each of the criteria. Some jurisdictions have experienced delays with the authorization process, owing to incomplete or substandard application materials being submitted. This is neither a good use of the Authority's resources in needing to chase up missing material, and ultimately delays the authorization process for the applicant.

To mitigate the above risks, the Authority will have regard in the first instance to the completeness of the application materials submitted. Should it determine that the materials provided do not meet the specified criteria and requested information, the Authority will exercise its power under the proposed VASP Act to refuse the application and the application fee will be forfeited.

On the other hand, if a complete application pack is submitted and the applicant has failed to demonstrate to the Authority that it has the necessary measures, understanding, experience, tools and other pertinent requirement; the Authority will have the power to reject the application and bar them from a period of 6 months. As with the refusal, the application fee will be forfeit. Similar to the motivations described above, the 6 months bar is intended to mitigate the risk of applicants immediately

reapplying, without having invested sufficient time and resources to address the measures or controls found to be insufficient to meet the authorization requirements in the first instance.

Substance Requirements

A number of participant discussions centred around the proposed substance requirements, especially proposed variations to the requirements that would apply to applicants operating as an international business company (IBC).³

IBC and Directorship Requirements

The IBC Act presently only requires a single director in order to be incorporated. Nonetheless, for licencing purposes a minimum of two directors will be necessary for a VASP. The difficulty to meet the requirement of one individual director being on island was raised. However, this requirement shall remain. As noted in the policy paper, the requirements in the draft bill are designed to mitigate specific risks to which the Seychelles could be exposed to when authorising VASPs. Cases in other jurisdictions have shown that oversight and governance of VASPs are critical controls to ensuring that financial crime risks are understood and effectively mitigated. The jurisdiction has assessed that allowing VASPs to be authorised based on a single director who may be comprised of a legal entity located overseas, would not be an appropriate governance model.

Furthermore, it would not permit the Authority to effectively oversee and verify that the requisite time, expertise and resources were being allocated to ensure the VASP was being effectively overseen and governed. The Authority acknowledges the potential limitation which may be faced when trying to find FAPs with the appropriate level of expertise and knowledge, especially in relation to the Seychelles' AML/CFT requirements, to fulfil the role of VASP directors. Entities applying for a VASP licence may avail themselves of the services presently offered by CSPs, which include directorship services, however, this will be subject to the Authority ensuring that the individual has capacity and the necessary competence to serve as such. Further guidance will be provided by the Authority as to the type of training, experience and/ or expertise which it would consider sufficient to meet these requirements.

Directorships and Existing Licensed Securities Dealers (SDs)

For existing SDs licensed under the Securities Act, there will not be an obligation to have an additional two directors for the purpose of fulfilling this licence obligation. However, the current directors will have to demonstrate, to the satisfaction of the Authority, that they are capable of fulfilling the role for the purposes of both licences.

Availability of Qualified Personnel

Certain existing players spoke about their willingness to import foreign talent to satisfy some of the substance requirements but questioned as to the feasibility and ease of doing so. The Authority will be engaging with Immigration and the Ministry of Foreign Affairs to determine the possibility of e-visa's for the sector. It is acknowledged that, at present, only certain high positions allow for individuals to be accompanied by their dependents, and not all persons would be embodying such roles. This is a long-term plan, however, there is a current framework in place which allows for persons in certain positions access to the jurisdiction in order to fulfil these roles.

Meetings

Feedback was received with regards to the in-person board meetings being a requirement, more specifically the frequency. The FSA has taken same into consideration and revised this requirement to a minimum of two (2) board meetings in Seychelles, on a quorate basis.

³ i.e. with no physical presence in the jurisdiction, save for the Registered Office and Agent.

Other Substance Requirements

Other areas of concern centred around the requirement that client onboarding, opening of bank accounts and insurance coverage must be undertaken, opened, and obtained in Seychelles. The Authority has made the determination to allow for client onboarding to be undertaken elsewhere on the condition that all data and related AML/CFT information collected and maintained from client onboarding is accessible from the Seychelles, in accordance with the substance requirements.

It was further impressed upon participants, that the VASP itself will remain wholly responsible and liable for both meeting the authorization requirements, maintaining them post-authorization and ensuring that they are conducted in compliance with the AML/CFT Act and Regulations. The licenced VASP will be held liable and any applicable enforcement action will be taken against them for non-compliance with these requirements.

Discussion by and between the Central Bank, allowed for further clarity as to the local banks current risk appetite for opening of bank accounts, with the Central Bank advising that at the moment only 2 financial institutions are ready and willing to offer such services. Whilst the Central Bank made clear that they will not be prohibiting local banks from opening bank accounts for VASPs, the same will be dependent on the individual bank's risk appetite. With those realities in mind, the Authority has opted to revise its position and omit the local bank account requirement at this time and will consider revising this requirement so that the applicant must evidence it had opened an account in a jurisdiction that subscribes to at least Basel II requirements. This will ensure that a level of security measures and AML/CFT adherence is maintained and will facilitate exchange of information requests. However, this may be subject to change at a later stage if it is found that the ML/TF risks emerge and a different approach is required, to ensure effective mitigation.

Overall, no objections were raised concerning the substance requirements regarding the handling of customer complaints from the Seychelles. This requirement is also linked to the record-keeping requirements, so as to ensure these records are retained and retrieved in a timely manner and provided to authorities, when so requested.

Questions were raised as to whether domestic insurers have a sufficient understanding of the product to be able to offer relevant and appropriate insurance covers. At the moment, local insurers are offering Professional Indemnity Covers to existing licensees under the Securities Act, however, the Authority intends to open a line of communication to better gauge the providers ability to make such an offering available to VASPs. Whilst this may take time to settle on a final position, the Authority will not be requiring that insurance coverage be sourced from the Seychelles. It will be permissible to obtain cover from another jurisdiction, provided that same is sufficient and covers the extent of the permissible activities under a VASP licence. There may be an element of discretion that will be exercised by the Authority for an applicant operating under a larger group structure. However, it will be for the VASP to demonstrate that they have appropriate coverage, to the satisfaction of the Authority, both at the time of authorisation and thereafter. Alongside the legislation, the Authority will issue guidelines for licensing which will further clarify what is acceptable in this respect.

Market Conduct and Prudential Supervision

General feedback in respect to the market conduct and prudential supervision requirements was positive, with most of the proposed measures already being in place for existing licensees overseen by the Authority in the Seychelles. Nonetheless, the Authority will ensure that further guidance is provided concerning market conduct, conduct of business requirements within the relevant regulations, supplemented by additional guidelines.

Monitoring of Unauthorised Activity

A number of press releases have been published by the Authority in its own capacity, as well as in conjunction with other relevant government authorities like the Registrar of Companies, denouncing entities that have claimed to be affiliated or licenced by the Seychelles, containing lists of both those who are entirely unknown to the Seychelles regulatory bodies, as well as those who are. The collaborative efforts will continue, so as to put the public on notice and safeguard the reputation of the Seychelles as a Financial Services Sector.

The Authority reiterated throughout the consultation process that following expiry of the transition period at the end of December 2024, timely action will be taken to identify VASP operating without authorization. The FSA will take the necessary enforcement action if and when unauthorised actors are found to be operating in the sector.

Enforcement Process

In view that the FSA is leveraging its existing mechanisms and internal processes to effectively regulate and supervise VASP activities; no feedback was received in terms of the proposed enforcement process and was therefore deemed to be acceptable to participants.

Preventive Actions

No comments were received concerning this section of the policy paper.

AML/CFT Considerations

Record Retention

A number of questions from participants centred around the *modus operandi* for record retention, namely since VASPs are a technology-based service providers, whether cloud storage solutions would be permissible. The Authority acknowledges the standard business model applied by VASPs in employing cloud storage. While the Authority will not prohibit the use of cloud storage, measures must be in place to ensure that such storage measures are secure and that data can be readily accessed and retrieved from the Seychelles, in accordance with the substance requirements. Applicants will therefore be expected to demonstrate, as part of the authorization process, how their data is stored, and that operationally, data related to client onboarding, transaction monitoring, transfer activity and other related information, can be retrieved and accessed in real time from the Seychelles. Further information regarding these requirements will be elaborated upon in additional guidelines.

Third Party Relationships

It was initially proposed that the AML/CFT Act be amended to prohibit VASPs licenced in the Seychelles from relying upon third parties to undertake any controls required to detect and mitigate financial crime risks. VASP participants explained the various operating models employed by them, which in some cases includes reliance upon other group members to fulfil these requirements. One participant asked whether using a RegTech solution provider, that makes available software used to screen client names, for example, would also constitute third party reliance.

Both the Authority and the Financial Intelligence Unit (FIU) are aware there have been cases in other jurisdictions whereby VASPs have employed weak or ineffective AML/ CFT controls, owing to a lack of proper oversight of third parties contacted to undertake these activities. In some cases, this has meant Authorities have been unable to obtain information in a timely manner, for both domestic and overseas cases conducting investigations into suspicious or illegal activity.

The results of the ONRA indicated that the Seychelles may be vulnerable to the misuse of VA and VASPs, in part due to its lack of access to relevant AML/ CFT information, so as to permit timely and effective investigation of suspected illicit activity.

The Authority appreciates that some VASPs may have arrangements in place with external providers to support their AML/CFT activities. However, as a matter of effective governance and oversight, and owing to the jurisdiction's understood financial crime risk exposure in this sector, it will require VASPs authorised in the Seychelles to either directly conduct their AML/CFT activities or be able to demonstrate that those activities are undertaken by a corporate entity which forms a part of their group structure.

The Authority will reserve the right to refuse authorization of a VASP, where it determines that group arrangements involve a corporate entity in a jurisdiction which does not have commensurate AML/CFT requirements to the Seychelles or has a legal framework which prevents or compromises the ability to effectively exchange information or obtain cooperation for investigation purposes.

The Authority and FIU will monitor compliance with this requirement during the first year of the VASP Act's enactment. Further feedback will be obtained from the newly formed VASP Working Group and thematic examinations, to evaluate the implementation of this requirement and whether reliance upon unrelated external third parties should be permitted.

One participant requested clarification whether the reference to “third party relationships” included counterparty VASP for the purpose of the FATF travel rule. FATF guidance requires VASPs to conduct third-party due diligence on their counterparts for AML/CFT purposes prior to, or at the time of, the first transaction order, so as to mitigate financial crime risks. The Authority agrees that counterparty VASP relationships can involve multiple entities within a counterpart's group, which may have their own AML/CFT requirements to address potential ML/TF risks to which they could be exposed. Steps will be taken to update the AML/CFT Regulations to require that VASPs undertake due diligence and maintain ongoing monitoring of counterparties, in accordance with FATF guidance.

It was impressed upon attendees that the use of tools or technology-based solutions will not be deemed to amount to reliance on third parties. However, the FSA and FIU expressed concerns as to the licensees solely employing tools to fulfil their CDD and KYC, with emphasis as to the collection and retention of data. Further information regarding how the FSA expects VASPs to fulfil AML/CFT requirements will be elaborated upon in additional guidelines.

Unhosted Wallets

One participant noted there was no reference to the expected treatment of unhosted wallets. VASPs will be expected to adopt a risk-based approach when dealing with unhosted wallet transfers. They should obtain further information on the unhosted wallet on a risk-basis. In higher risk cases, VASPs should consider taking further steps to ascertain the source of funds in the unhosted wallet and authorise the transfer only if the control over the unhosted wallet can be reasonably established. The treatment of unhosted wallets will be elaborated upon further in the AML/ CFT Regulations.

Sanction Screening

One participant noted that the proposed amendments concerning sanction screening required review and update to also include screening and freezing obligations upon beneficiary VASPs, and a requirement to respond to requests for information to assist in sanction screening disposition, in accordance with national data privacy requirements. The provisions in the AML/CFT Act will be updated to incorporate these requirements.

Travel Rule

In general, the participants acknowledge understanding the need for the Seychelles to reflect implementation of what are known as the “Travel Rule” requirements, which form part of FATF Recommendation 15 and related guidance. However, some participants noted that the requirement for contemporaneous collection of identifier information to satisfy this Rule, has not been operationally possible for most VASPs, owing to limitations in the method by which this information can be exchanged between originator and beneficiary intermediaries.

The purpose behind the Authority's proposal for contemporaneous exchange is to ensure a timely effort is made to obtain and receive the identifier information associated with VA transfers. Whilst, the Authority acknowledges that contemporaneous collection would exceed the current FATF Travel Rule requirements, the proposed requirements will be updated to require that this data be provided without delay in alignment with Recommendation 15's requirement. VASPs will be expected to have second line controls that include regular testing to verify that identifier data has been collected for transfers received or sent. It will also be expected that where VASPs rely upon a third-party provider's technology to obtain and exchange identifier data, the VASP must have controls in place to verify that the provider collects and can facilitate the exchange of identifier data required under the Seychelles AML/ CFT legislation.

Some participants noted that they may conduct transfers with counterparties who may be based in a jurisdiction where Travel Rule requirements may differ or who may know yet be required to apply them. The Seychelles, as an international finance centre, is vulnerable to possible misuse by illicit actors who may seek to use the jurisdiction to launder the proceeds of criminal activity. This may include using VASPs operating in the Seychelles to layer or further distance VAs used for this purpose, from its originating source. Both the VASP and the authorities' ability to investigate suspicious transfers, is greatly limited without having the requisite identifier information. Therefore, while the Authority will not prescribe that a specific third party provider (often referred to as a “bridge”) be used, the onus will be placed upon authorised VASPs to ensure that by whatever mechanism is employed, identifier information for originators and beneficiaries is obtained in accordance with the AML/ CFT Act and that such information is accessible and retrievable in the Seychelles.

Some parties raised concerns regarding the requirement that IP address data also be collected with respect to customers and the transfers undertaken for them. Operational concerns and overall utility of this data, relative to the value received from it, was identified as a reason for not requiring its mandatory collection. The Authority is mindful that the analysis from the July 2022 ONRA identified that there have been cases where the Seychelles has been linked to alleged illicit activity, originating from a counterparty VASP in a different jurisdiction. More broadly, VASP cases have often been linked to parties who attempt to obscure the originating geographic nexus of funds, by moving VA across exchanges in different jurisdiction.

It is not the intent of the Authority to suggest that only IP address data should be collected and retained. The Authority acknowledges the challenges in contemporaneously exchanging this information at the time a transfer takes place. However, effective AML/CFT and sanctions compliance controls require the collection, authentication, and monitoring of multi-source location data points. VASPs will be expected not to solely rely upon IP addresses for this purpose but to also use more reliable and accurate location indicators. Beneficiary VASPs will be expected to have taken reasonable steps to determine the jurisdiction of the originator, especially where the VASP may have group entities trading under similar names in other or multiple jurisdictions. Therefore, the simultaneous transmission of IP address data along with other data points required by the Travel Rule will not be required, but VASPs will be expected to capture and retain both IP address and other location data points. This will be described further in both the AML/ CFT Regulations and future guidelines.

Whilst the Authority acknowledges that collection of IP addresses extends the FATF guidelines, this information has proven to be more useful for investigations, enforcement and identification of users.

Additionally, attention was drawn to the fact that most VASPs in other jurisdictions currently make use of third-party compliance tools in order to satisfy the travel rule obligation. The decision to undertake business with VASPs operating in jurisdictions that do not apply Travel Rules, is a risk decision for the VASP itself. With consideration had to the Seychelles' risk appetite, given its vulnerability for misuse by persons outside of the jurisdiction and the possibility parties making use of these VASPs to conceal their identity and source the funds effectively circumventing the Travel Rule requirements.

Further clarification and guidance was sought as to what is meant by originator and beneficiary wallet address. Same will be catered for more specifically within guidance.

Dual Reporting Requirement

Some VASP participants expressed concerns regarding the dual suspicious activity report (SAR) proposed requirement. The basis of these concerns was that this would create a heavy operational burden on the VASPs to manage dual filing for every cross-border transfer for which a SAR is needed.

In preparing the proposed VA and VASP legislative framework, the Technical AML/CFT Working Group reviewed data concerning detection of suspicious activity linked to Seychelles. Regard was also had to the experience of some jurisdictions where VASPs were authorised in more than one jurisdiction in terms of how and to whom SARs were reported. The Working Group found that in some instances, SARs with a nexus to the Seychelles, were not reported to the FIU, despite the VASP operating in the jurisdiction. In some cases, this appeared attributable to the lack of reporting requirement for VASPs under the AML/CFT Act. In other instances, however, it appeared there was a risk that VASPs were limiting their reporting to the jurisdiction in which they were licensed, regardless of the nexus to the Seychelles.

This exposes the Seychelles to the vulnerability that it will not be made aware of suspicious activity, allowing for a timely and effective response by authorities. The intention of the proposed provision is therefore not to require reporting to the counterparty VASP, but rather to ensure that all reports of possible suspicious activity, where a possible nexus to the Seychelles is identified, are reported to the Seychelles FIU, in accordance with the AML/CFT Act. This should include instances where a counterparty or sister company make a VASP authorised in the Seychelles, aware of suspicious activity linked to the Seychelles. It will be a matter for VASPs authorised in the Seychelles to determine, where a nexus may exist with jurisdictions where it may also hold authorization, to make a similar disclosure to the national FIU there.

Treatment for Licensees under Securities Act

With the potential overlap between the services presently offered by licensees under the Securities Act, and the activities to be governed by the draft bill, concerns were raised as to whether or not they will have to obtain a second licence, whether licensee will have to maintain separate entities for operations and licencing purposes, whether additional authorisations will be required if offering trades in contract for differences (“CFDs”) where the underlying asset is a virtual asset and whether a VASP license would necessary if accepting payment in VA.

With consideration as to licensing, if a current licensee under the Securities Act wishes to undertake any of the regulated VASP activities then a second license must be applied and obtained in order to do so. The Authority further advised as to the ability for the existing two directors (as is required under the Securities Act), to fulfil the role for the purpose of obtaining a VASP licence provided that they are able to demonstrate the necessary competency, capability and other fitness and propriety requirements to serve as director on a VASP. In short, there will be no added requirement to have four (4) directors (2

for the SD licence and 2 for the VASP licence), but rather 2 competent, FAP individuals will be able to sit in post. Concurrently, existing SDs will be required to update internal documents, which will include but not be limited to manuals, internal controls etc to incorporate the additional risk associated with VA-linked activities.

Where the establishment of separate entity is concerned, there are arguments that could be made in terms of preserving established individuality whilst divorcing risks associated with the respective activities. The Authority will not impose any obligation as to chosen structure. It will be a matter for the applicant itself to determine, whether to operate the VA-linked services under its current corporate umbrella or to do so via a separate legal entity provided that it is a domestic company or IBC.

SDs accepting payments through e-wallets directly or via regulated VASP exchanges will be required to obtain a licence under the proposed VASP Act. SDs should have regard to the list of activities at the start of this response, which the Authority will treat as falling within the scope of the proposed VASP Act.

SDs further voiced concerns about current offerings where the investment tool is underpinned by VA (e.g. CFDs), and whether any additional authorisation under the VASP ACT would be necessary to continue trade these instruments. With the Securities Act governing the activities and types of securities which may be traded, paired with the relatively broad definition provided for CFDs, no policy decision has been made as to their treatment. Whilst it is acknowledged that there is an element of VA involved, further research and study is required to determine the appropriate treatment. The Authority will prepare a policy paper and proposal to be published and consulted on by latest December 2024. Until then, the status quo around these products will be maintained.

With respect to the paid up capital requirements, whilst there were little to no issue around the proposed amounts to be maintained, existing licensees under the Securities Act enquired whether this was to be compounded within their existing capital requirements, or whether this will be an additional requirement. The proposed treatment would be for separate accounts to be maintained, in order to segregate each licensable activity's capital, in that same will not be consolidated within a single account, nor will the current amount maintained be deemed sufficient for VASP licensing purposes.

Tax Matters

Noting the additional requirements imposed upon VASPs operating using an IBC, participants queried the impact of these requirements upon those entities eligibility to retain the preferential tax rate. Further questions were raised as to what the overall business tax rate would apply to VASPs operating in or from the Seychelles.

The Ministry of Finance and the Seychelles Revenue Commission are presently working on a scenario analysis following which the country will issue a pronouncement prior to the VASP Act coming into effect. The proposal conveyed however, is to mirror the present SD regime and allow for some form of tax concession. No official position has been reached yet. A final position on the question of business tax will be taken prior to the enactment of the VASP Act, so that the VASPs can decide whether to apply for authorization, on a fully informed basis regarding their possible tax liability.

Other Matters Raised

Auditors

On the subject of Auditors, participants recommended that they retain the ability to appoint foreign auditors due to limited resources, understanding and experience of the product within the Seychelles. The Authority, under the Securities Act, presently approves for the appointment of foreign auditors. However, the issue presently arises in that the Registrar of Companies does not accept submission of

those audited accounts, but rather only accept that which have been prepared by local auditors duly licenced by the Seychelles Licencing Authority.

The Authority acknowledges the difficulties faced in appointing competent and experienced auditors and the fact that most VASP's will be or intends to form part of a group and the pooling of resources is a common occurrence. Note has been taken and further engagement has been made with the Registrar of Companies. Further guidance will be provided in the licencing regulations.

In further regard to audited accounts, recommendations were made as to the submission deadline, with some asking for flexibility for same. Whilst the Authority is in agreement, to do away with a set date and allow for submission to be effected within 6 months of the end of the financial year, late submissions will be subject to enforcement action.

Sensitization

Participants raised the important consideration about the need for sensitization and education of the public. Recommendations included continuing the programme to educate the public about the risks associated with VAs, and notably, the promotion of such investments on social media or through multi-level marketing schemes. In partnership with the Central Bank of Seychelles, an educational and sensitization campaign has been launched in the fourth quarter of 2023. The CBS has driven the initial campaign with the FSA to pick up and continue running same in 2024.

The proposed public campaign will include educational materials on the authorities various platforms e.g. Instagram and websites, whilst also targeting local outlets to run informative sessions. The ONRA, found a lacking in the understanding of both everyday individual and people within the financial services sector, around VAs and VASPs in general.

Further Regulations

Some participants enquired whether the Authority planned to undertake further consultation on the above referenced requirements, once they have been further described in regulations or guidance. Seychelles is currently working to an agreed deadline for enactment and introduction of the VASP legal framework by no later than the end of March 2024. Mindful that feedback received from this initial consultation has proven valuable in formulating updates to the framework, the Authority will endeavour to coordinate written consultation on key regulations so that applicants are fully aware of the application requirements and criteria which must be satisfied for authorization, along with further details concerning fulfilment of the AML/ CFT legislative obligations.