

FAC Regulatory Impact Summary

Policy and Approach

FAC policy is to take a compliance first approach and innovate within the existing regulatory rails.

The proposed FAC distributed ledger platform for funds servicing introduces new technologies and redefines some roles whilst maintaining support for existing regulations through three core principles:

1. **Delivered by Authorised Businesses** - FAC is not seeking regulated status for itself, the network will be operated by an established market infrastructure provider and participants will all be existing regulated businesses in the UK
2. **Launch Regulated Funds** - Funds launched on the FAC network will be regulated ICVC funds incorporated under the UK OEIC regulations 2001
3. **Protect Regulatory Oversight** - The roles defined in the FCA Handbook section COLL 6 relating to the Authorised Fund Manager and Depositary are unchanged and will retain responsibility for regulatory compliance of funds launched on the FAC network.

FAC product design and implementation is guided by the **FAC legal and regulatory advisory group** which is made up of industry and legal professionals with significant experience in advising and managing regulated businesses in the UK.

As part of our pilot planning a wider legal and regulatory working party will ensure a broader understanding and validation of FAC regulatory compliance and align with operational and technical preparations for the pilot.

Overview of regulatory and legal landscape

This table summarises FAC's understanding of the regulations, laws and guidance that apply to its design and operation.

Functional Area	Roles	Relevant Regulations
Fund Lifecycle (Launch – Closure)	Fund Manager, Depositary, ACD, Registrar	FCA Coll3, UK OEIC Regulations 2001, MIFIDII
Investor Activity	Investors, Registrar, Nominee/Custodian Cash Exchange	Money Laundering Regulations and Criminal Finances Act 2017, FCA CASS Rules, GDPR, MIFID II (suitability / Costs and charges)
Fund Servicing	Fund Administrator, Registrar, Fund Manager, Depositary and Fund Custodian, Cash Exchange, Network Operator	FCA Coll6 CP19/32 - FCA Guidance on Operational Resilience ISO27001 – Information Security Management GDPR
Investment Manager Activity	Fund Manager, ACD Depositary and Fund Custodian, Cash Exchange	FCA Coll 3 MIFID II
Fund Oversight	ACD, Fund Manager, Depositary, Regulator	FCA Coll3 UK OEIC Regulations 2001
Distributed ledger and crypto technology	All parties involved in issuing or trading in crypto assets, registering crypto asset trades or involved in the oversight of these activities	CP19/22 - FCA Guidance on Digital Assets LawTech Panel Review on legal status of cryptoassets and smart contracts AMLD5 for Digital Asset Service Providers and FATF guidance on Virtual Assets and Virtual Asset Service Providers

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Key Regulatory Focus Areas

This list is a summary of key regulatory considerations for FAC. A detailed legal and regulatory issues list is maintained by FAC.

Focus Area	Understanding / Assumptions	To be reviewed / Legal advice needed
Fund setup and oversight	<ul style="list-style-type: none"> Funds can launch as UK regulated ICVC entity under the UK OEIC regulations 2001 That the existing responsibilities of the ACD, Fund Manager and Depository can be fulfilled for funds operating on FAC 	<ul style="list-style-type: none"> Validate that we can launch a tokenised fund share and operate a distributed ledger under an OEIC umbrella Validate that an existing OEIC umbrella can be used to launch a tokenised share class and/or tokenise an existing share class in a split register Validate roles and responsibilities defined within the regs are maintained
KYC/AML	<ul style="list-style-type: none"> That KYC/AML responsibilities can be undertaken 'at the boundary' of the network on the investor node and can be shared with other entities on the network requiring confirmation of an investors identity That the Network Operator will KYC node operators when joining the network and the node operator then has responsibility for any investors they introduce to the network via their node That the Network Operator does not have any AML responsibilities 	<ul style="list-style-type: none"> Validate the 'boundary and shared' approach and define the mechanisms by which an agreed KYC/AML approach can be adopted by all FAC participants Fully define the role and responsibilities of the network operator in relation to KYC/AML responsibilities
Client Money and Cash Tokenisation	<ul style="list-style-type: none"> That a FAC cash token has the same legal status as a fiat currency and is regulated in the same way That the responsibilities of an ACD can be delegated to a network Cash Exchange operator That once cash tokens are issued cash held by a cash exchange is no longer client money but held in safekeeping against the tokens issued on the network That a cash exchange operator must be a licenced deposit taker approved by the Bank of England Existing regulated entities approved for operating with fiat currency do not require a separate authorisation to operate as a digital asset service provider under AMLD5/FATF rules That a regulated fund can issue cash tokens through a cash exchange backed by its own cash assets for the purpose of settling investor transactions That a regulated fund can maintain as part of its assets an 'on ledger' box or other liquidity pool of cash tokens held for the purposes of managing investor settlement 	<ul style="list-style-type: none"> Further analysis required to confirm the operating structure and mandate of a cash exchange and its relationship with the ACD of a fund operating on the FAC network Further analysis required to confirm issuance and accounting practices for funds settling investors trades in cash tokens Understand how regulations relating to digital asset service providers impact FAC participants
Asset Tokenisation	<ul style="list-style-type: none"> That a tokenised fund share class will be regulated as a security by the FCA That a regulated fund constituted as a UK OEIC can issue a digital tokenised share and that the regulation of this will be the same as a conventionally issued share That the owner of a FAC issued fund token will be considered the registered owner of the value in the fund represented by that token That a fund can hold on ledger a box or store of issued tokens that are held for the purposes of managing investor settlement 	<ul style="list-style-type: none"> Validate a regulated fund company can issue shares as digital tokens Validate the operating model, risks and liabilities related to a fund holding a box or other such pool of issued fund tokens
Distributed ledger	<ul style="list-style-type: none"> That the role of maintaining a share register for a regulated fund currently performed by a transfer agent can be distributed across investor and fund nodes That ownership of tokens on the network identifies the registered owner of the fund share That delivery of tokens is required to update the register and to finalise the change of title on a share That a transfer agent must retain a right to compel an investor to surrender their tokens in the event a fund closure or merger 	<ul style="list-style-type: none"> Understand the impact on the Transfer Agents role, risk and liability resulting from the distribution of data across a network of participants Validate that the methods used to maintain and share data across a distributed ledger preserve the integrity and status of the register in law. Is delivery legally enforceable? Can an investor who cannot deliver their tokens be considered to have lost the value of

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	<ul style="list-style-type: none"> That the transfer agents responsibility to ensure the operational resilience of their processes and integrity of the register is limited on a distributed ledger and that responsibilities and liabilities will need to be shared across network participants and the network operator. 	those tokens and any rights over the shares altogether?
Private Key Security	<ul style="list-style-type: none"> That the security of private keys is a critical requirement for all participants of a distributed network That custody of investor assets on FAC will be interpreted as custody of the private keys that control those assets That there are currently no officially sanctioned guidelines or standards that apply to key management in a financial services context Assume FAC will have to adhere to the highest level of security practice in relation to private keys and security of nodes 	<ul style="list-style-type: none"> Further analysis needed to define the standards that FAC node operators will be required to adhere to and the contingent risks and liabilities associated with this Confirm UK stance on key management as aa custodial service Further definition of the responsibilities and powers of the network operator to enforce security controls on network participants and revoke their participation
Smart Contracts	<ul style="list-style-type: none"> That transactions undertaken on the FAC network will be legally enforceable That final settlement on ledger by exchange of tokens will be considered legal final settlement of the contract 	<ul style="list-style-type: none"> Review and define existing fund terms and conditions to ensure a FAC transaction is legally enforceable. Define a template application for a new investor to a fund and a contract note.