



# RECOMMENDATIONS:

FOR COUNTRIES AND VIRTUAL  
ASSETS SERVICE PROVIDERS ON THE  
VIRTUAL ASSETS PLAYING FIELD

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# INTRODUCTION



Developments in recent years, in the field of new technologies, namely, with respect to the 4.0 Industrial Revolution in general, and blockchain in particular, have contributed to the advent of new products and services, have disrupted traditional financial services, and pose challenges for countries and organizations.

The deregulation associated with these new products and services presents high risks, in terms of criminality and economic stability, making it essential to understand the advantages and risks associated with virtual assets (VA) and virtual assets service providers (VASP).

Kismet's main objective is to set the standards on VA and VASP and to promote their implementation at strategic, legal and regulatory, and operational levels for an effective VA ecosystem.

Kismet's standard creation and enforcement contributes to a broader strategy on VA and VASP regarding the management of the associated risks. The final goal is to ensure a leveled playing field for VA and for VASP and to identify those, who pose significant threats to the financial industry.

## **Approach overview**

Kismet's approach to VA and VASP is based on a comprehensive and integrated set of methodologies, which countries and VASP should adopt and implement in order to create an adequate VA ecosystem, consisting of:

- Conceptual framework
- Recommendations
- Risk assessment methodology

- Rating methodology.



In the conceptual framework, the different concepts related to VA and VASP are defined, to facilitate a broad understanding about complex concepts, by providing a common language, between the different key actors and between them and all the other stakeholders.

The Recommendations establish the basic principles for the implementation and management of a VA ecosystem, at strategic, legal and regulatory level, as well as regarding operational and risk management, aiming for medium and long-term sustainability.

The risk assessment methodology defines the set of risks to be analyzed to assess the correct adoption and implementation of the

Recommendations. For each risk identified, this methodology evaluates if a set of mitigating measures are in place, to calculate the VASP's risk exposure.

The rating methodology allows, based on the risk assessment methodology, to assign a rating to VASP, to demonstrate their level of adoption and implementation of the Recommendations, and measuring its effectiveness.

Kismet is committed to building a close and constructive dialogue with countries and VASP, other international stakeholders and national authorities, to protect the VA ecosystem and promote best practices regarding these assets.

This document contains Kismet's Recommendations.

## **About Kismet**

Kismet, a company under Dutch law, is a leading organization in providing rating for virtual assets service providers on the virtual assets playing field. Kismet's approach and rating solutions, help countries and VASP increase trust and credibility and enable stakeholders to identify opportunities, manage the risks of doing business with VA, and make better decisions.

Kismet's people are from diverse generations and varied cultural backgrounds. They have solid academic and distinct professional experience, which allows for a multidisciplinary and transversal approach to the VA ecosystem.

For more information about Kismet, visit [kismetconsulting.eu](https://kismetconsulting.eu).

# 1 | UNIVERSAL STANDARDS



# **101 | Foundations**

## **101-1 | Design of the Recommendations**

In the Recommendations, different dimensions are considered, to obtain an integrated view, namely the organizational, legal, financial, economic, environmental, social, and political dimensions, from a sustainability perspective of the VA ecosystem.

Whenever possible, it was decided to refer to the international standards, relevant to each of the dimensions or subdimensions, with the respective adaptation to the reality under analysis. In this way, among others, GRI standards were adopted for the analysis of different sustainability issues, ISO 37001 for anti-corruption; and FATF standards for anti-money laundering.

The Recommendations intend to enhance the credibility of VA and VASP, and the confidence of the markets and its different stakeholders.

## **101-2 | Organization of the Recommendations**

The Recommendations are divided into three series:

- universal standards (100 series)
- countries (200 series)
- VASP (300 series).



Universal standards are principles of general application, which provide an adequate understanding of the intended results by the different stakeholders, aiming at the harmonization of the interpretation and implementation of Recommendations by countries and VASP.

The country-specific Recommendations intend to define the principles underlying the strategy to VA, the definition of the legal and regulatory framework, and the risk management associated with VA and VASP, for a well-functioning VA ecosystem.

The specific Recommendations for VASP, aim at the implementation of an adequate control and risk management structure, for the various activities, products, and services, as well as the audibility and the promotion of transparency and integrity.

## **102 | Application principles**

The application of the Recommendations, by countries and VASP, should consider their specific reality.

For the proper application of the Recommendations, countries and VASP must:

- understand their own specific context related to VA
- validate the applicability of the Recommendations to the specific situation
- identify its key stakeholders and how to respond appropriately to their legitimate interests and expectations
- validate the auditability of the options taken and of the respective reasoning.

The countries and VASP should adapt the Recommendations to their particular circumstances. Whenever a Recommendation is not applicable to the specific context of a country or VASP, an explanation must be provided.

## **102-1 | Information standards**

In order to be aligned with the Recommendations, the countries and the VASP, must demonstrate the respective implementation, and justify their respective options.

The disclosure of information must be supported by qualitative and quantitative data, and respect the following requirements:

- timeliness and correctness
- clarity and consistency
- auditability.

## **102-2 | Consistency between Recommendations**

The decisions related to the implementation of the Recommendations, must take into account the Recommendations as a whole, in the definition of the implementation approach and respective reasoning. The goal should be to guarantee the coherence, completeness and consistency in the respective implementation or the justification of the respective impossibility.

# 2 | COUNTRIES



## **201 | Context of the country**

Countries should have a risk and context document, relating to VA and VASP, which identifies national specificities and associated opportunities and risks, which should be considered for the purposes of preparing the VA strategy and the national risk assessment.

A framework of the different types of VASP and their activities, products and services must also be presented.

## **202 | VA strategy**

Countries should draw up a strategy to VA and VASP, that includes a clear vision for VA and VASP, describes priorities and expected results, offers a timeframe for implementation, and analyzes the benefits and risks of the approach.

The strategy should address legal and regulatory, operational, and technical aspects and consider the implementing capacity of the country and VASP.

It should also address the regulation and inspection requirements, as well as the cooperation needs between the different key actors, at national and international level.

## 203 | National risk assessment

The national risk assessment should provide a factual overview of the current situation concerning VA and VASP.

The risk assessment shall examine both VA and VASP, and cover at least the following aspects:

- legal and regulatory description, assessment, and analysis of the current legal and regulatory framework that has direct and indirect impact on VA and VASP
- operational description, assessment, and analysis of the national framework regarding VA, including a clear mapping of responsibilities of each key actor involved in the VA ecosystem
- technical description, assessment, and analysis of the current technology as well as the functionalities covered by the current systems, to work with VA.

Based on the conclusions of the risk assessment, the countries should perform a SWOT analysis of the current legal, operational, and technical aspects. The analysis should consider, among others, the consistency, impact, or potential constraints of the current aspects, including loopholes.

Countries should require VASP to identify, assess and take effective measures to protect the VA ecosystem.

## 204 | Legal and regulatory framework

Countries should establish a legal and regulatory framework, which allows the definition of the fundamental concepts related to VA and VASP, and of the rules for the respective operational framework.

## **204-1 | VA definition**

Countries should establish a definition of VA, as a digital representation of value that can be traded or transferred, highlighting their respective categories and underlying technology.

## **204-2 | VASP definition**

Countries should establish a definition of VASP, whether natural or legal persons, highlighting its different types based on the products and services provided, and underlying technology.

## **204-3 | VASP licensing or registration**

Countries should ensure that VASP are licensed or registered, regardless of whether they are registered or operating in the country, and subject to effective regulatory and supervisory measures.

## **205 | Regulation and supervision**

Countries should establish powers and responsibilities for regulators and supervisors and ensure that VASP are subject to adequate regulation and supervision.

## **205-1 | Power of supervisors**

Supervisors must have adequate powers to supervise and monitor the performance of VASP, and ensure that they comply with legal and regulatory requirements and best practices.

## **205-2 | Guidance and feedback**

Regulators and supervisors should issue guidance on VA, that enables VASP to adopt adequate operational and risk management models.

## **206 | Coordination and cooperation**

Countries should designate an authority to coordinate the VA ecosystem. That authority should be responsible for the coordination of VA policies and for the national risk assessment.

Countries should promote internal and international cooperation, between the different authorities, as well as between these and VASP, and ensure that they can cooperate rapidly and efficiently.

The exchange of information, concerning the development and implementations of VA policies and operational frameworks, should be encouraged.

# 3 | VASP





## **301 | Context of the VASP**

VASP shall determine the external and internal matters that are relevant to its purpose and that impact its capability to attain goals.

Some of the matters to be determined include, but are not limited to, the following:

- entities over which the VASP has control and entities which exercise control over the VASP
- size, structure and delegated decision-making authority of the VASP
- locations and sectors in which the VASP operates
- business model
- nature, scale and complexity of the VASP's activities and operations
- applicable statutory, regulatory, contractual and professional obligations and duties.

## **302 | Corporate strategy**

VASP should draw up a strategy, that includes a clear vision, describes priorities and expected results, offers a timeframe for implementation, and analyzes the benefits and risk of the approach.

The strategy should address legal and regulatory, operational, and technical aspects and consider the implementing capacity of the VASP.

## **303 | Governance**

### **303-1 | Governing bodies and top management**

VASP must define and disclose the governance structure of their organization as well as the composition of the highest governance body and its committees by:

- executive and non-executive members
- independence
- tenure on the governance body
- other significant positions and commitments held by each member of the governance bodies and the nature of those positions and commitments
- gender
- membership of under-represented social groups
- competencies relating to economic, environmental and social topics.

VASP leadership must be composed of elements that have the right skills and backgrounds to properly insure the governance of the organization.

Moreover, VASP governing bodies and top management must demonstrate their commitment with respect to the organization's strategy, policies and management systems.

### **303-2 | Fit and proper**

VASP must have in place procedures to perform assessments of the fit and proper of members of the management body, both in its management

function, executive positions, and in its supervisory function, non-executive positions.

### **303-3 | Expectation of stakeholders**

VASP must ensure that the process of stakeholder engagement is robust, in order to bring accountability to its boards and governing bodies. A successful stakeholder engagement process should identify all relevant stakeholders, proactively solicit their involvement, and describe the frequency and method of engagement.

VASP shall determine:

- stakeholders that are relevant to the organization, these must include all individuals, groups of individuals or organizations that affect and/or are affected by the organization's activities, products or services
- communication channels and frequency of engagement for each stakeholder category
- reasonable expectation and interests of each stakeholder groups and how the organization addresses them.

## **304 | Economics and financials**

### **304-1 | Market presence**

VASP should report several market presence indicators such as the markets served, the location of the headquarters and the main operations,

the scale of the organization, as well as a description of their products and services per market.

## **304-2 | Economic performance**

VASP must disclose economic performance indicators, such as the value generated and distributed, in the form of financial statements that convey the business activities and the financial performance.

Additionally, VASP must consider the financial regulatory and reporting requirements of the context in which they operate.

## **304-3 | Indirect economic impacts**

VASP should assess and communicate the indirect economic impacts of their activity in accordance with *Disclosure 203-2 Significant indirect economic impacts* of the GRI Sustainability Reporting Standards 2016.

According to GRI's disclosure, VASP shall report the following information:

- examples of significant identified indirect economic impacts of the organization, including positive and negative impacts
- significance of the indirect economic impacts in the context of external benchmarks and stakeholder priorities, such as national and international standards, protocols, and policy agendas.

## **304-4 | Financial controls**

VASP shall implement financial controls that manage the financial risks of the VA environment.

## **305 | Operational**

VASP must implement the appropriate mechanisms for an efficient management of the organization's operations.

### **305-1 | Planning and control**

VASP must plan the necessary processes to meet the requirements of the management systems, implement the actions set by those plans, and establish the necessary control processes to implement the actions determined in the corporate strategy.

### **305-2 | Non-financial controls**

VASP must implement non-financial controls to manage and mitigate non-financial risks with respect to areas as operations, sales, procurement, human resources.

## **306 | Technological**

VASP should implement the appropriate systems and functionalities to work with their activities, products and services.

## **307 | Anti-financial crime**

VASP should have an integrated, coherent and assertive approach to anti-financial crime, both at preventive and detective levels, ensuring the proper implementation of policies, processes and controls, aiming at the timely detection and appropriate treatment of the identified risks.

### **307-1 | Anti-financial crime policy**

VASP should define an appropriate anti-financial crime policy and ensure its effective application.

The anti-financial crime must be adequate to the nature, size, complexity, and activity of the VASP and include, at least:

- risk management model
- procedures and controls
- technical systems and tools
- awareness and training programs
- suitability and effectiveness testing mechanisms.

## **307-2 | Anti-financial crime management system**

VASP must define an anti-financial crime management system, which includes:

- the governance structure and the respective internal reporting channels
- the mandate and the type of tasks to be performed
- the necessary human resources, required skillset and any necessary means for operational and technical support.

VASP must guarantee the effective implementation of the anti-financial crime management system, and proceed to the respective evaluation, through realization of the appropriate tests to the effectiveness of the implemented controls, according to the anti-financial crime policy.

## **307-3 | Anti-corruption**

VASP must comply with the applicable legal and regulatory anti-corruption framework and be aligned with the international best practices.

### **307-3a | Corruption risk-assessment**

VASP must identify, assess, and take effective action to mitigate the corruption risks in the context of their specific reality, namely with regard to the following factors:

- nature, size, and complexity of the business relationship
- type of counterparties involved and associated risk
- geographical factors.

VASP should assess risk by:

- applying a risk-based approach
- determining the degree of probability and impact of each of the identified risks
- assessing the overall risk level
- defining risk mitigations measures and controls
- determining the frequency of risk review.

### **307-3b | Procurement due diligence**

VASP should pay special attention to the risk of corruption at the procurement level, related to the supply of products and services, both in relation to direct suppliers and the respective supply chain.

VASP should carry out procurement due diligence, in accordance with the Due diligence recommendation of ISO 37001.

According to ISO's Recommendation, whenever the application of the corruption risk assessment results higher than low risk, regarding the nature and extent of the risk associated with the type of business and counterparties due diligence must be carried out.

Due diligence must also be carried out, in each specific case, in relation to the different stakeholders, with the necessary depth and frequency, to obtain adequate information for an effective corruption risk management.



## **307-4 | Anti-money laundering and counter terrorism financing**

VASP must comply with the applicable legal and regulatory anti-money laundering and counter terrorism financing framework and be aligned with the international best practices.

### **307-4a | Money laundering and terrorism financing risk assessment**

VASP must identify, assess, and take effective action to mitigate the money laundering and terrorist financing risks in the context of their specific reality, namely with regard to the following factors:

- nature, size, and complexity of the activity pursued
- type of VA involved
- products and services provided
- distribution channels
- counterparties risk
- geographical factors.

VASP should assess risk by:

- applying a risk-based approach
- determining the degree of probability and impact of each of the identified risks
- assessing the overall risk level
- defining risk mitigations measures and controls
- determining the frequency of risk review.

## **307-4b | Customer due diligence**

VASP should undertake customer due diligence measures in accordance with FATF Recommendation 10.

According to FATF's Recommendation, when establishing a business relationship or carrying out occasional transactions, VASP should:

- identify the customer and verify his identity
- identify the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner
- understand the ownership and control structure of the legal persons
- understand and obtain information on the purpose and intended nature of the business relationship
- conduct ongoing due diligence on the business relationship and scrutiny of transactions undertaken, to ensure the consistency between that and the knowledge of the customer, their business and risk profile, including, where necessary, the source of funds.

The VASP should determine the extent of the due diligence measures in accordance with the risk of the customer.

## **307-4c | Sanctions**

VASP must ensure that they do not establish business relationships with sanctioned entities, whether natural or legal persons, through the application of the necessary measures and mechanisms for their identification and report, in an appropriate and effective way.

### **307-4d | Political exposed persons**

VASP should identify the politically exposed persons and ensure that they are monitored in accordance with an appropriate risk analysis.

The monitoring of the business relationship must:

- take reasonable measures to establish the source of wealth and source of funds
- conduct enhance ongoing monitoring of the relationship.

### **307-4e | Transparency and beneficial ownership**

VASP must ensure an adequate understanding of the ownership and control structure of legal persons.

Before establishing a business relationship or conducting an occasional transaction, VASP must:

- adopt all necessary measures to assess the status of the beneficial owner
- obtain information on the identity of the beneficial owner
- adopt of reasonable measures to verify the identity.

VASP must also identify the beneficial owner, whenever the counterparty is a natural person who may not be acting on his own behalf.

### **307-4f | Monitoring of activities and transactions**

Whenever VASP detects the existence of any conduct, activity, or operation, which due to its atypicality, may be related to money

laundering and/or terrorism financing, they should examine them with special attention, intensifying the degree and nature of the monitoring.

### **307-4g | Suspicious transactions report**

VASP should report promptly to the competent authorities any suspicions they have, regarding activities and transactions that may involve funds from illicit sources.

## **308 | Risk and compliance**

VASP must implement the appropriate mechanisms for an efficient risk and compliance management.

### **308-1 | Compliance function**

The VASP must define a model of the compliance function that shall cover at least the following aspects:

- governance structure of the compliance function and the respective internal reporting channels
- mandate and the type of tasks to be performed by the compliance function
- necessary human resources, required skillset and any necessary means for operational and technical support.

## **308-2 | Risk-based approach**

VASPs must apply a risk-based approach, with the aim of ensuring a legal and regulatory compliance, as well as an effective risk management.

This approach should contribute to an efficient allocation of resources.

### **308-2a | Risk assessment**

The risk assessment should provide a factual overview of the current situation concerning compliance risks of the VASP and its activity:

The risk assessment shall cover as minimum the following aspects:

- legal and regulatory description, assessment, and analysis of the current legal and regulatory framework that has direct and indirect impact on VASP and its activity
- organizational description, assessment, and analysis of the internal framework within the VASP, including a clear mapping of responsibilities of each key actor involved in the risk management
- operational description, assessment, and analysis of every stage of the VASP operational activities, and existing measures to detect and mitigate risks, covering synergies with other VA ecosystem stakeholders, such as regulators and law enforcement
- technical description, assessment, and analysis of the current technology as well as the functionalities covered by the current systems, to work with VA.

Based on the conclusions of the risk assessment, the VASP should perform a SWOT analysis of the current legal and regulatory, organizational, operational, and technical aspects. The analysis should consider, among

other aspects, the consistency, impact, or potential constraints of the current aspects, including legal and regulatory, organizational, operational, and technical loopholes.

### **308-2b | Risk mitigation plan and controls**

VASP should have a risk mitigation plan, which should consider all aspects analyzed in the risk assessment, and must include, as a minimum:

- a description of the mitigating measures and respective activities to be undertaken by the VASP
- guidance on the specific steps needed to mitigate risk
- the key actors responsible for each step, and other relevant stakeholders whose participation is deemed important for the successful implementation of each step.

The VASP is expected to prepare a monitoring and evaluation framework on the implementation and management of the risk mitigation plan. The framework should include a list of key performance indicators and a set of controls and evaluation criteria.

### **308-3 | Data privacy and security practices**

VASP must comply with all legal requirements and regulations regarding data privacy and security practices applicable in their context of operations, and developing the appropriate policies to manage these issues. These policies should be aligned with the best standards.

## **308-4 | Marketing and labelling**

VASP must comply with specific marketing and labelling laws and regulations concerning their specific products and services.

Additionally, VASP must disclose the incidents of non-compliance with these regulations concerning products and services information and labeling.

## **308-5 | Record-keeping and auditability**

VASP should keep for at least five years, all necessary records to enable them to comply with information requests from competent authorities. Such records must be sufficient to permit the reconstruction of the activities and operations, and to provide, if necessary, evidence for prosecution of criminal activity.

## **308-6 | Awareness and training**

VASP should invest in training, educating and reskilling their workforce. Trainings should include issues such as the organization's values and ethical conduct policies, data privacy policies, cybersecurity policies, anti-bribery and anti-money laundering policies and other significant organizational policies as well as new skills and tools trainings. Moreover, training on the technologies and programs necessary to the VASP activities must be provide to all relevant employees that work with those.

VASP shall document the training procedures, the content of the training, and when and to whom it was provided, reporting the average hours of

training per person that the organization's employees have undertaken during the reporting period, by gender and employee category.

## **309 | Environmental**

VASP shall measure and mitigate the negative environmental impacts of their activity and comply with environmental laws and regulations existing in their context of operations.

### **309-1 | Energy**

VASP must monitor, assess, and report their energy consumption in accordance with *Disclosures 302-1 and 302-2 Energy consumption within the organization and Energy consumption outside of the organization*, of the GRI Sustainability Reporting Standards 2016.

According to GRI's disclosure, VASP shall report the following information:

*Disclosure 302-1 Energy consumption within the organization:*

- total fuel consumption within the organization from non-renewable sources, in joules or multiples, and including fuel types used
- total fuel consumption within the organization from renewable sources, in joules or multiples, and including fuel types used
  - in joules, watt-hours or multiples, the total electricity consumption, heating consumption, cooling consumption, steam consumption
  - in joules, watt-hours or multiples, the total electricity sold, heating sold, cooling sold, steam sold
- total energy consumption within the organization, in joules or multiples



- standards, methodologies, assumptions, and/or calculation tools used
- source of the conversion factors used.

*Disclosure 302-2 Energy consumption outside of the organization:*

- energy consumption outside of the organization, in joules or multiples
- standards, methodologies, assumptions, and/or calculation tools used
- source of the conversion factors used.

## **309-2 | Environmental compliance**

VASP must comply with environmental laws and regulations applicable to their context of operations. Environmental compliance includes compliance with international declarations, conventions and treaties, as well as national, sub-national, regional, and local regulations.

Moreover, VASP must disclose information regarding significant fines and non-monetary sanctions for non-compliance with environmental laws and regulations.

## **309-3 | Supplier environmental assessment**

VASP must have a supplier due diligence process in place designed to prevent and mitigate negative environmental impacts in the supply chain. Suppliers' environmental due diligence can include assessment for several different environmental criteria such as impacts related to energy, emissions, water or compliance with environmental laws and regulations.

## **310 | Social**

VASP shall have human resources processes in place that insure a decent and inclusive work environment for all employees, as well as measure and mitigate the negative social impacts of their activity and comply with social laws and regulations applicable to their context of operations.

### **310-1 | Employment process**

VASP shall determine their approach to employment, which comprises the processes set in place for hiring, recruiting and retention. Moreover, VASP shall determine the working conditions provided, making sure that they contribute for decent and fair work for all employees.

### **310-2 | Diversity and inclusion**

VASP should have policies in place that insure equitable opportunities to all employees in recruitment and selection, training, development and promotion. These policies should ensure that no employee is discriminated for or affected by their gender, race, age, ethnicity and sexual orientation.

In this context, VASP must report the percentage of employees per employee category, age group, gender and other indicators of diversity, as well as the number of discrimination and harassment incidents, status of the incidents and actions taken.

### **310-3 | Supplier social assessment**

VASP must have a supplier due diligence process in place designed to prevent and mitigate negative social impacts in the supply chain.

Suppliers' social due diligence can include assessment for several different environmental criteria such as human rights; employment practices; health and safety practices; discrimination incidents; wages and compensation; and working hours.

### **310-4 | Social compliance**

VASP must comply with social laws and regulations existing in their context of operations. Social compliance includes compliance with international declarations, conventions and treaties, as well as national, sub-national, regional, and local regulations.

Moreover, VASP must disclose information regarding significant fines and non-monetary sanctions for non-compliance with social laws and regulations.

### **310-5 | Literacy in VA**

VASP should empower their clients and society in general through initiatives that promote the possession of the set of skills and knowledge that allows an individual to make informed and effective decisions with all of their VA.

Additionally, VASP are recommended to report initiatives supported or promoted regarding Literacy in VA, their objectives, public audience and frequency.

