

FINNIUS

The first step towards regulating (the trade in) cryptos?

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 4 MINUTES

On 14 May 2018, a new package with measures aimed at intensifying the battle against money laundering and terrorist financing was approved at a European level (in the market often referred to as the fifth Anti Money Laundering Directive). One of the new measures entails that (i) cryptocurrency exchange platforms and cryptocurrency brokers and (ii) custodian wallet providers (jointly: crypto service providers) will fall within the scope of the framework for anti-money laundering.

These rules will eventually be implemented in the Money Laundering and Terrorist Financing (Prevention) Act (Wet ter voorkoming van witwassen en financieren van terrorisme, Wwft). This means in practice that these crypto service providers have to comply with the Wwft. The most important obligation pursuant to the Wwft is that crypto service providers have to perform customer due diligence with respect to all their business relationships (in any case the brokers on the cryptocurrency exchange platform and the holder of the wallet). Furthermore, crypto service providers have to monitor all transactions and, if necessary, notify the Financial Intelligence Unit (FIU) of any unusual transactions. The new rules also provide for an obligation for crypto service providers to register. Currently, it is not clear what this obligation to register will look like and where crypto service providers should register.

As far as we are concerned, the introduction of these new rules is a positive development. Currently, trading in cryptos finds itself in a somewhat grey area, partly due to the lack of regulation. Supervisory authorities issue warnings on a regular basis about a variety of risks surrounding the trade in cryptos; for example fraud, the sensitivity for money laundering, extreme volatility, and the lack of supervision, transparency and information. Currently, there is no framework in place to address these risks, while it seems that cryptos, at least for the short term, are here to stay. There even appears to be an increasing interest from investors in cryptos. In my opinion, it is important for both crypto service providers as well as existing financial market participants that some form of regulation is implemented in order to address the risks as much as possible.

One of the main risks frequently identified is that the trade in cryptos – because of the anonymous nature of cryptocurrencies – is sensitive to money laundering and terrorist financing. By bringing the trade in crypto under the scope of the anti-money laundering framework, especially the link where it is possible to convert cryptos into fiat money, this issue could be largely addressed. This would entail that crypto service providers have to act as gatekeepers for the trade in cryptos. The AFM or DNB will most likely oversee this gatekeeper role.

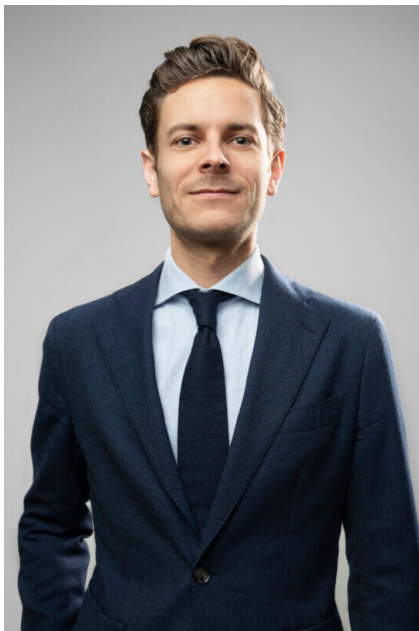
Perhaps this could be a reason for banks and payment institutions to enter into business relationships with crypto service providers (again) in order to, inter alia, open a bank account. A concern often heard in the market is that at the moment it is virtually impossible to open a bank account as a crypto service provider. In view of the unclear status of the trade in cryptos and the frequent warnings of supervisory authorities (also directly addressed to banks) and the costs

associated with mitigating the risks, this may be – from a commercial and compliance point of view – a prudent choice from the perspective of the financial market parties. These new rules may potentially offer a solution for both the crypto service providers and for existing financial market parties.

The European Commission has opted for a rather short implementation period according to European standards. Member States must transpose the new rules into national law within 18 months. This means that the new rules must enter into force by the end of 2019. This is of course under the assumption that the Netherlands will make the implementation deadline. After all, the Fourth Anti-Money Laundering Directive should have been implemented on 26 June 2017, but this has not happened yet.

Having said all the above, with these new anti-money laundering rules, we are not there yet. Another frequently heard risk is that cryptos (including so-called initial coin offerings (ICOs)) are not regulated and parties that facilitate their issue and trading are not subject to supervision or any other set of rules. There seems to be a need (from regulators, supervisors and the market alike) for regulation and supervision, precisely because the innovative character of cryptos and the underlying blockchain is recognised. This was also clear during a debate in the Dutch House of Representatives, where various motions were passed along these lines (innovative and supervision is desirable). We are curious about how this will develop in the future. It is our prediction that one of the biggest challenges will be to develop regulation that can address the cross-border nature of (trading in) cryptos.

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