Regulation of Cryptocurrencies

Some thoughts on where we are and where we might go
Does it matter?

**Yes**
- Unregulated
- Untraceable
- Used by money launderers
- Used by drug cartels
- Used by terrorists
- Used by anyone wanting to hide money

**No**
- Insignificant volumes to be meaningful
- Disproportionate effort for risk involved
- Lack of real evidence to support claims made
- Do we really understand the risks and how to address them?
Cryptocurrency, is it a viable investment opportunity for the wealth management industry?

▪ “As bitcoin and other cryptocurrencies are not legal monetary tender issued by central banks, many respondents voiced deep-seated concerns about their viability as a financial instrument.”

▪ “When asked whether they would promote cryptocurrencies to their clients as a viable – even if alternative – asset class, respondents voiced concerns about the lack of regulation, while others worry about the difficulty in understanding the instrument. Some fear that unscrupulous IT gurus could manipulate their valuation.”
Cryptocurrency, is it a viable investment opportunity for the wealth management industry?

- “Could cryptocurrencies become a mainstream asset class? Virtually all the respondents who replied directly to that question stated an emphatic ‘no’, certainly not as things stand today. But, most were confident that the blockchain technology facilitating bitcoin – and many other cryptocurrencies – would have widespread, dramatic implications for transactions in everyday life in the future.”
Cryptocurrency, is it a viable investment opportunity for the wealth management industry?

▪ “Earlier this year [2017], Japan’s authorities approved bitcoin as a legal payment.”

▪ “Not all jurisdictions are so crypto positive, with Indonesia the latest country to ban bitcoin transactions, which [took] effect on January 1, 2018.”
Some basics

Cryptocurrency, is it a viable investment opportunity for the wealth management industry?

- “In short, the regulatory, financial and reputational risks associated with cryptocurrencies remain too great. “At most, it is a currency, at worst a bubble of epic proportions akin to tulip mania”. Some feel that the extreme volatility and less than transparent pricing of the different varieties of cryptocurrencies precludes it from being a valid asset at this stage.”

- “Not a single respondent said they would advise clients to invest in bitcoin or alternatives.”

- “With one of them even stating: “The difference between investment and gambling is whether we can conduct fundamental evaluation”. ”
"Bitcoin has long been the transaction currency of choice for drug dealers and extortionists, but this month, the IRS has upped the game. Just as tax evasion finally took down Al Capone, now the IRS is looking for tax evaders and other tax cheats who have been using Bitcoin in an attempt to hide their tracks."

"…the only reason Bitcoin has value to anyone is because of the underlying value as a medium of exchange for lawbreakers."

"Is Bitcoin in fact tied to the growth of ransomware? “It’s helping. I think that’s definitely true,” says David Emm, Senior Security Researcher at Kaspersky Lab. “The existence of effectively anonymised payment mechanisms definitely plays into the hands of cybercriminals.”

Putin considers ‘cryptorouble’ as Moscow seeks to evade sanctions

- The Financial Times reports that Russian government is considering using its own cryptocurrency for “sensitive activity on behalf of the state”...

- It also reports that it will enable the Russian government to avoid sanction

Source: https://www.ft.com/content/54d026d8-e4cc-11e7-97e2-916d4fbc0da?desktop=true&segmentId=7c8f09b9-9b61-4fbb-9430-9208a9e233c8
So where are we on regulation?

MAS cautions against investments in cryptocurrencies

The Monetary Authority of Singapore advises the public to act with extreme caution and understand the significant risks they take on if they choose to invest in cryptocurrencies.

- MAS considers the recent surge in the prices of cryptocurrencies to be driven by speculation. The risk of a sharp reduction in prices is high. Investors in cryptocurrencies should be aware that they run the risk of losing all their capital.

- There is no regulatory safeguard for investments in cryptocurrencies. As in most jurisdictions, MAS does not regulate cryptocurrencies. Nor do MAS regulations extend to the safety and soundness of cryptocurrency intermediaries or the proper processing of cryptocurrency transactions.
So where are we on regulation?

MAS cautions against investments in cryptocurrencies

- As most operators of platforms on which cryptocurrencies are traded do not have a presence in Singapore, it would be difficult to verify their authenticity or credibility. There is greater risk of fraud when investors deal with entities whose backgrounds and operations cannot be easily verified.

- Cryptocurrency transactions are generally anonymous, which makes them vulnerable to being misused for unlawful activities. If a cryptocurrency intermediary is found to have used cryptocurrencies illegally, its operations could be shut down by law enforcement agencies. There is also a risk of loss should the cryptocurrency intermediary be hacked, as it may not have sufficiently robust security features.
China has declared the hottest part of the cryptocurrency market “illegal”

- The sale of cryptographic tokens, a market that has boomed this year, has been deemed an “illegal fundraising practice” by China’s central bank. In a notice published today, the regulator ordered all such offerings to be halted, for exchanges to stop trading in the tokens, and for funds already raised to be returned to investors.

- The crypto industry’s official line is that more regulation is good. The new regulations are “good for the whole community,” because they will weed out scams from legitimate offerings.

So where are we on regulation?

**Regulator warns Bitcoin buyers: Be ready to lose all your money**

- Andrew Bailey, head of the Financial Conduct Authority, told the BBC that neither central banks nor the government stood behind the "currency" and therefore it was not a secure investment.

- Buying Bitcoin, he said, was similar to gambling - and had the same level of risk. "It's not a currency, it's actually not regulated in its Bitcoin form"

- "We know relatively little about what informs the price of Bitcoin."

- "It's an odd commodity as well, as the supply is fixed."

- "If you want to invest in Bitcoin be prepared to lose your money - that would be my serious warning."

So where are we on regulation?

**ECB governor calls for tax, regulation on bitcoin**

- "One ought to apply what the basic rule is in any other financial transaction: everyone involved should reveal their identity," ECB governing council member Ewald Nowotny told the German daily Sueddeutsche Zeitung.

- "It can't be allowed that we've just decided to stop printing 500-euro notes to fight money laundering, that we've slapped strict rules on every tiny savings club, and then have to watch people blithely laundering money around the globe with bitcoin,"

What does all this mean?

- Like any tool it is open to misuse
- The risk of misuse will draw the attention of law makers/regulators/law enforcers
- By its nature it is not capable of being regulated directly
- So they approach the problem indirectly
- Currently these are normal controls applied to real currencies when converting from a cryptocurrency
Australia

- *Anti-Money Laundering and Counter-Terrorism Financing Amendment Act 2017* expands the existing legislation to include digital currency exchange providers. This will be in the form of mandatory registration and compliance obligations.

- The draft rules were published on 2 January and are subject to consultation closing on 6 February 2018

USA

- IRS summonses to target suspected tax evasion
The Australian approach is a relatively simple way forward
  - but, unless followed globally, will only move exchanges elsewhere

The US approach has the simplicity of treating cryptocurrencies as property and taxing profits as capital gains
  - but requires significant effort to chase down tax evaders
So where do we go from here?

- Cryptocurrencies are here to stay
- Some will be fraudulent
- Exchanges are the most vulnerable points in the system
- Anonymity or near anonymity will remain an issue
So where do we go from here?

Regulators are divided on the route to take, current options are:

- Digital currencies are banned
- Some regulation of digital currencies
- No regulation of digital currencies
- Encouraging of digital currencies
So where do we go from here?

Western regulators are more cautious

Major global banks take their lead from the “lead regulators”

Visa ends relationship with cryptocurrency provider

Many banks in Europe and the USA have a policy of de-risking by refusing business which they feel puts them at risk; eg Wafic Said, a Syrian born billionaire philanthropist and businessman “shunned” by Barclays

Options for moving forward

01
Treat cryptocurrencies as commodities not currency

02
Regulate Exchanges

03
Regulate access to Exchanges

04
Require Exchanges to submit transaction reports
The basics for effective regulation

- Must be a global regulatory standard
- Applied consistently
- Approach must address the risks cryptocurrencies represent
- Alternatively must address the needs of law enforcement to allow for effective action against wrongdoers / abusers