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AMLD5 AND CRYPTOCURRENCIES

OCTOBER 2018

One of the biggest threats associated with virtual currencies (or cryptocurrencies) is their potential use for money laundering and terrorist financing purposes. With the adoption of the 5th Anti-Money Laundering Directive ("AMLD5") on 30 May 2018, the European Union attempts, amongst other things, to address this issue.

Senders and recipients of virtual currencies can usually carry out these transactions anonymously.

Distributed ledgers (e.g. blockchains) on which these operations are carried out offer an anonymous yet (in principle) safe technical channel. There is no need to associate a specific identity to a virtual wallet or a transaction. Technically, no prior identification is required.

Besides, virtual currency transactions are not confined to specific jurisdictions. They are accepted roughly everywhere and do not require any centralised intermediary. Having Internet access is sufficient to send virtual currencies to the other side of the world.

These features of virtual currency transactions render the control on, and the interception of, these operations particularly tricky.

This is why, since a few years already, public authorities, notably at the European level, have been feeling the need for a new regulatory approach.

In its opinion (2014/08) of 4 July 2014 on virtual currencies, the European Banking Authority ("**EBA**"), advocated for a whole set of measures to address the risks of virtual currencies.

These measures included for instance:

- the compulsory creation/licencing of a "scheme governance authority" for each virtual currency which would be in charge of its integrity;
- the extension of the market abuse and AML rules to virtual currency transactions;
- the enactment of specific rules of conduct for market participants.

Taking into account the complexity and the highly resource-intensive nature of the proposed comprehensive regulatory approach, and the urgent need for a quick regulatory response to virtual currencies, the EBA recommended, in the short run, to extend the personal scope of the AML Directives to the virtual currencies exchange providers (the "**VCEPs**"), i.e. providers engaged in exchange services between virtual currencies and fiat currencies).

AMLD4 and virtual currencies

Triggered by the November 2015 Paris attacks, the European Commission proposed to amend the 4th Anti-Money Laundering Directive (the "**AMLD4**") even before its transposition date (in principle on 26 June 2017[1]). Its proposal consisted of bringing the following two entities under the scope of AML rules by the beginning of 2017:

- the VCEPs; and
- the custodian wallet providers (the "**CWPs**"), i.e. entities that provide services to safeguard private cryptographic keys on behalf of their customers, to hold, store and transfer virtual currencies.

Finally, the AMLD4 was not modified prior to its transposition, notably because the EBA itself advocated for an extension of the initial deadline (to allow both public authorities and businesses to adapt) in a second opinion on virtual currencies (2016/07) of 11 August 2016.

Nevertheless, these discussions paved the way for the changes brought by the AMLD5.

Regulatory approach of the AMLD5

One of the main innovations of the AMLD5 is to give a legal definition to virtual currencies.

Art. 1, (2), d) of the AMLD5 defines a virtual currency as "a digital representation of value that is not issued or guaranteed by a central bank or a public authority, is not necessarily attached to a legally established currency, and does not possess a legal status of currency or money, but is accepted by natural or legal persons, as a means of exchange, and which can be transferred, stored and traded electronically".

Following the abovementioned propositions, the approach of the European legislator to regulate the use of virtual currencies consisted of including VCEPs and CWPs in the list of obliged entities regulated by AML rules.

Consequently, these new obliged entities will become subject to regulatory requirements similar to those of banks, payment institutions and other financial institutions.

For instance, they will be required to implement necessary customer due diligence controls, to monitor transactions and to report any suspicious activity to the relevant national authorities (i.e. the Financial Intelligence Processing Unit in Belgium).

The new obliged entities will also be subject to a registration obligation.

Through these obliged entities, the European legislator hopes that competent authorities will be able to monitor the use of virtual currencies.

However, the EU legislator admitted that this new approach would not entirely fix the problem of anonymity attached to cryptocurrency transactions since users can still execute these transactions without VCEPs and CWPs, thereby bypassing the new regulatory framework (recital 9 of AMLD5).

Only the beginning of the virtual currency regulation?

The AMLD5 must be implemented into national law before 10 January 2020.

However, the EU legislator is already aware of the fact that this new regulatory framework will not be sufficient to tackle AML issues in relation to virtual currencies. By 11 January 2022, the EU Commission has been mandated to examine and, as the case may be, draft legislative proposals regarding self-declaration by virtual currency owners and regarding the maintaining by the Member States of central databases registering users' identities and wallet addresses.

It is likely that, sooner than later, other European legislative initiatives will come to cover other aspects of virtual currencies, e.g. the licencing of

[1] Member States had committed to transposing the AMLD4 before the transposition deadline. Belgium finally transposed the AMLD4 in the law of 18 September 2017.

"scheme governing authorities", or the use of virtual currencies as payment or investment means.

Besides, it is worth noting that the Member States do not necessarily wait for European initiatives and that some (fragmented) measures have already been adopted at national levels.

For instance, the FSMA issued a ban on the sale of derivatives products whose values derive from virtual currency to retail clients.

Existing regulations could also apply to virtual currencies. Though many legal uncertainties remain, the FSMA considers that some initial coins offerings can be subject to the rules of the law of 16 June 2006 on public offers (see its Communication 2017/20 of 13 November 2017).

It is also not excluded that some virtual currencies should be considered as "electronic money" in the meaning of Directive 2009/110/EC.

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For more information on virtual currencies, ICOs, blockchain and EU legislative initiatives in these fields, please contact ***Simont Braun's Digital Finance Team*** *(digitalfinance@simontbraun.eu).*