

New AML/CTF Regulations for Cryptocurrency exchanges

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In brief

Global cryptocurrency regulation is a varied landscape, with some countries implementing outright bans on Initial Coin Offerings, and others setting out to become 'blockchain islands'. Australia appears to recognise cryptocurrency is here to stay and has introduced regulatory oversight by amending Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) laws to cover Australian digital currency exchanges. The Australian Transaction Reports and Analysis Centre (AUSTRAC) commenced regulatory oversight on 3 April 2018. Despite many applauding the new laws as a boost to consumer confidence in the budding digital currency industry, some believe regulating exchanges will merely chase investors offshore in search of friendlier jurisdictions. This LegalTalk Alert explores the potential impact of Australia's new AML/CTF regulation of cryptocurrency.

In detail

New AML/CTF Laws

On 3 April 2018, AUSTRAC commenced regulation of digital currency exchanges (DCEs) under new AML/CTF laws in Australia made through amendments to the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) (**the Act**).

Who and what is covered?

The new laws apply to anyone who provides a registrable digital currency exchange service. This covers any service that involves the exchange of any fiat currency, whether Australian dollars or not, to cryptocurrency and vice versa. The service must be provided in the course of carrying on a digital currency exchange business.

Cryptocurrency, or 'digital currency', is defined as a 'digital representation of value that functions as a medium of exchange, a store of economic value, or a unit of account'. Digital currency is also defined as being publicly available, interchangeable with money, able to be used for consideration and not government-issued. This definition excludes money in closed gaming environments and any government-issued cryptocurrencies that may exist in the future. The AML/CTF laws may also be amended at a later date to identify specific digital currencies that fit, or do not fit, within the definition.



Once registered, DCEs are subject to AML/CTF compliance and reporting obligations. DCEs will be required to collect and store information on customers' identities and transactions, have a system to monitor suspicious activity, report any suspicious transactions over AUD10,000 and establish an AML/CTF compliance program. With many smaller exchanges in start-up phase, the cost and technical knowledge required to implement and maintain an adequate AML/CTF compliance program will be challenging, and could lead to the larger exchanges gaining further market prominence.

DCEs may apply to the AUSTRAC CEO for exemptions from any of the provisions, although it remains to be seen whether the AUSTRAC CEO would grant any such exemptions.

Time limits for registration

All DCEs must be registered with AUSTRAC by 14 May 2018. After that date, new exchanges will be required to register before beginning their business operations. Registration must be renewed every three years.

From 3 April to 2 October 2018, AUSTRAC will implement a 'policy principles period' during which a DCE will not be subject to enforcement action as long as it is taking 'reasonable steps' to implement these compliance obligations. After the period expires, all DCEs must be registered and be compliant. This 'policy principles period' gives DCEs time to establish an AML/CTF compliance program and implement the necessary procedures to support ongoing AML/CTF compliance.

**14 May 2018
is the
deadline to
register
with
AUSTRAC**

Penalties for non-compliance

Under section 76A of the Act, a person can face up to two years' imprisonment, a fine of up to AUD105,000, or both, for providing unregistered DCE services, or if they breach a condition of their registration. The penalty doubles if the breach occurs after receiving compliance directions from the AUSTRAC CEO or there is a breach of a compliance undertaking.

If a second breach occurs, the penalty increases to seven years' imprisonment, AUD420,000 or both.

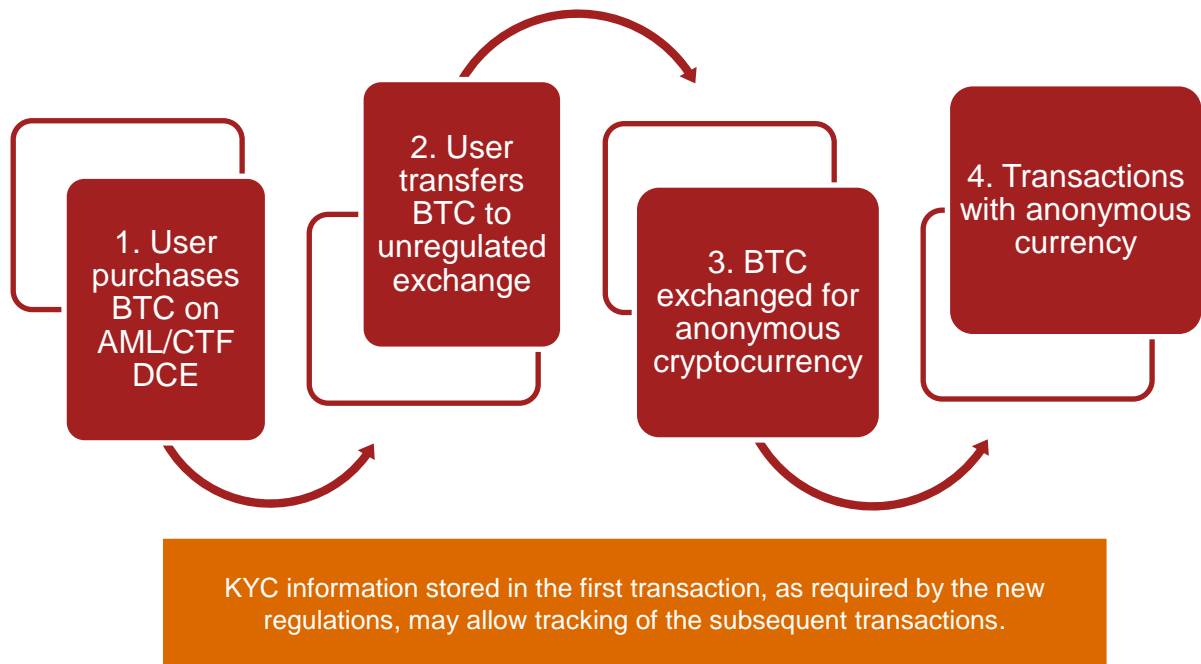
Market response to regulation

Australian DCEs appear to welcome the new laws. There are currently seven major DCEs operating in Australia, and within the first two weeks of implementation, four of them have received licences from AUSTRAC (Blockbid, Bid Trade, BTC Markets and Independent Reserve). Blockbid, which is preparing to open in 2019, is the first DCE to prospectively register.

Cryptocurrency analysts also tend to agree that AML/CTF laws will boost consumer confidence and promote the adoption of cryptocurrencies into mainstream transactions. The uptick in confidence will come from participants knowing that these new laws allow AUSTRAC to monitor Australian exchanges and probe into large-value cryptocurrency to fiat transactions, which until now have remained unchecked.

Even crypto-to-crypto exchanges which are excluded from the new laws are likely to be impacted as it would still be possible to track a user's information on a crypto-to-crypto exchange if the initial fiat-to-currency transaction occurred on an AML/CTF regulated exchange. Purchases of 'completely anonymous' cryptocurrencies, such as Monero, may therefore be capable of being tracked.

Is this the end of anonymous trading?



Whilst the Australian market will be better protected through regulation, there are still foreign alternatives for crypto investors looking to remain anonymous. It will be interesting to monitor the account activity at Australian DCEs in the coming months to identify any trends. The foreign DCE market includes more than 100 DCEs that allow Australians to purchase cryptocurrencies without AML/CTF checks. Users can also use VPNs to mask their geographical location to open accounts through these DCEs or when purchasing cryptocurrencies.

However, AML/CTF compliance is becoming a norm globally in crypto-regulation and, as each new jurisdiction jumps on board with regulation, the window of opportunity for fully anonymous cryptocurrency purchases appears to be narrowing.

The potential flight risk

While there is risk that some investors head offshore, up and coming DCEs themselves may also leave for friendlier jurisdictions. OKEEx, one of the world's largest exchanges, packed up operations in Hong Kong and moved to the 'blockchain island' of Malta following China's clampdown on cryptocurrency trading. Bitfinex, also in Hong Kong, is looking to move to Switzerland, a country self-described as a 'cryptocurrency haven'.

One of Australia's most successful DCEs, CoinJar, relocated to London in 2014 citing an unwelcoming regulatory environment as the reason. At that time, Australian banks had closed 17 DCE accounts in order to comply with their own AML/CTF obligations.

Whilst some jurisdictions pose more minimum regulatory requirements on cryptocurrency platforms, the overall global landscape is changing.

Under the European Union's Fourth Anti-Money Laundering Directive (4AMLD) passed in June 2017, member states will have 18 months to begin AML/CTF regulatory oversight for cryptocurrency transactions. The US, Taiwan, Vietnam, India and many other jurisdictions have also passed, or are in the process of passing, laws that implement AML/CTF regulations for DCEs.

Some jurisdictions are taking an even harder stance. In January 2018, South Korea banned all anonymous cryptocurrency trading. China has seen the mass exodus of DCEs and in February 2018 released an AML Regulatory Framework that will apply not just to DCEs, but also to cryptocurrency miners and wallets.

The takeaway

Australia's new AML/CTF laws for DCEs came into effect on 3 April 2018. Existing DCEs have until 14 May 2018 to register with AUSTRAC while new exchanges will be required to register prior to opening their doors for business.

The new laws effectively bring DCEs under the scope of existing AML/CTF compliance and reporting obligations, which many financial institutions are subject to, and will require DCEs to incur costs and develop increased technical capability to ensure compliance. However, the new laws are in line with the global trend towards imposing AML/CTF regulations on cryptocurrency transactions. When considering the endgame for many cryptocurrencies is to achieve mainstream adoption, Australia's new laws should only help to promote the integrity of cryptocurrency trading within the broader marketplace.

AUSTRAC has released a guide for DCEs on preparing and implementing an AML/CTF program, which can be downloaded [here](#).

If you operate, or intend to operate, a DCE you can enrol for the AUSTRAC digital currency register [here](#).

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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