Where to next? The case for crypto asset regulation just got bigger

By Richard Rattue

18 Jun 2021

The alleged loss of some $3.6bn Bitcoin through Africrypt investment company brings home just how risky this asset class truly is. Such incredible loss, though unfortunately not yet falling under the Financial Services Conduct Authority's (FSCA's) direct responsibility is likely to impact the velocity of crypto-asset regulatory development.

Image: ©lightboxx - 123rf.com

The recent announcement by the Intergovernmental Fintech Working Group (IFWG) sheds light on its position on regulating crypto assets – and change in this arena couldn't come sooner. Through its new position paper, which may now be updated in light of this latest scandal, several principles are put forward and are at the core of the objectives of the IFWG. The main objective being protection against the risks of crypto-asset investing.

> *Investors are looking to recover money lost at Africrypt. #crypto-currency #liquidation https://t.co/Czl7np3fAX— ITWeb News Publication (@ITWeb) June 17, 2021*

Inherent risks

Through the current paper, the regulator will bring crypto assets into the South African regulatory fold in 'a phased and structured manner'. The risks associated with this volatile asset class stand.

Regardless of the status of regulation, investing in crypto assets is risky and there is a high chance of financial loss, as clearly evidenced by the most recent market abuse scandal, even though there is also a high chance of reward through great returns. Keep in mind that liquidity in the market very much matters when it comes to selling out, provided you have chosen a profitable option, so timing becomes another crucial element of getting crypto-asset investing right, and earning a profit safely. Choosing the right cryptocurrency investment to align with is also an essential component.

Due diligence has never been more important.

The principles that count

The IFWG outlines six key principles:

1. Crypto assets must be regulated appropriately.
2. An activities-based perspective must be maintained.
3. A risk-based approach to regulation crypto assets must be applied.
4. The IFWG encourages a truly collaborative approach to crypto asset regulation.
5. Digital and financial literacy must increase so consumers are aware of the inherent risks of crypto assets.
6. A continuously proactive and dynamic approach must be taken to monitoring and maintaining the crypto marketplace, particularly in line with international best practice in real time. This could include setting up industry bodies, as an example.

Regulation recommendations

The FSCA’s responsibility for market conduct supervision is to extend into the crypto asset space, but while the IFWG has made 25 suggestions within this roadmap so far to get closer to regulation, the paper reiterates that the IFWG does not endorse this asset class.

Their goal is to reduce risk through regulation and through the paper, their recommendations can be broken down into three key focus areas. These are anti-money laundering and dealing with the financing of terrorism, cross-border financial flows and the application of financial sector laws.

Current exchange control regulations do not explicitly include crypto assets but the South African Reserve Bank's Financial Surveillance Department (FinSurv) is certainly taking notice, particularly with daily crypto asset trading values in South Africa exceeding the R2bn mark at the beginning of this year. With the recent alleged losses far surpassing this figure, this really is a dynamic, if dangerous asset class that should be treated with extreme caution by potential investors.

The position paper states that ‘by gradually bringing crypto assets into the South African regulatory purview, the most pertinent and immediate risks that have been identified around AML, cross-border financial flows and consumer protection will be addressed.’ Relevant developments through bodies like the Basel Committee on Banking Supervision have further supported the drive to regulate crypto assets.

Crypto assets remain highly speculative at this time, and it is unlikely that this will change anytime soon, however, the regulatory wheels are turning and trying to bring this new asset class into the mainstream of the river.

For consumers who cannot wait for regulatory protection, the rules of old apply. Understanding and noting the risks and not simply focusing on the potential reward can be the first step to avoiding a crypto scam. Undertaking an appropriate due diligence remains the best start to a good crypto asset investment decision.

Crypto assets should be monitored closely if it piques your interest as an investment asset class. It’s a positive step that regulation has taken note of the trend towards this exciting asset class, with more protection for investors not too distant on the horizon. Compliance officers should also look to upskilling in preparation for new compliance requirements that are sure to arise.

Remember the old adage …. if it is TGTBT then it probably is.

ABOUT RICHARD RATTUE

Richard Rattue is MD/Compliance Officer at Compli-Serve SA.

- Where to next? The case for crypto-asset regulation just got bigger - 3 Sep 2021
- Where to next? The case for crypto asset regulation just got bigger - 18 Jun 2021
- Market conduct and treating the customer right - 25 Jul 2017

View my profile and articles...