

2021



# ECONOMIC REPORT

*Critical analysis and comment on IFCs  
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## EVOLUTION THROUGH INNOVATION

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## BLOCKCHAIN & CRYPTOCURRENCY

# Ireland Needs Clear Cryptocurrency Plan



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Cryptocurrencies, such as bitcoin, litecoin and Facebook's libra, have hit the news headlines over the last few years. While this emerging area of financial services is an important feature of Ireland's drive towards becoming a cashless society, their decentralised, borderless and anonymous nature has caught the attention of the Irish government and financial and data protection regulators. There is currently no stand-alone regulatory regime that applies to cryptocurrencies and crypto-assets in Ireland. Regulators are taking the first steps towards the regulation of the provision and exchange of cryptocurrencies. To protect consumers and investors, and to safeguard market integrity, Ireland needs a balanced plan for regulation that is comprehensive but does not hamper innovation.

### What Is A Cryptocurrency?

There is no harmonised definition of cryptocurrencies and commentators often use the terms 'virtual currencies', 'cryptocurrencies' and 'crypto-assets' interchangeably. For the purposes of this article, a crypto-asset refers to a digital representation of value, stored on a distributed ledger, which uses cryptography to secure the transaction. A cryptocurrency refers to a crypto-asset in the form of unregulated digital

money that a user can store, transfer and trade electronically as a medium of exchange.

### Risks

Cryptocurrencies and crypto-assets pose a number of novel risks for consumers and investors:

#### *Price volatility*

Cryptocurrencies can suffer from volatile exchange rates due to their speculative nature. Traditionally, central banks controlled currencies and monetary policy. Cryptocurrencies do not follow this stability-orientated approach and their large price fluctuations mean that users risk losing some or all of the money they invest.

#### *Loss of regulatory protection*

Unlike traditional money, users buying or holding cryptocurrencies do not have access to the information disclosure requirements, safeguards and guarantees that come with participating in regulated financial services. Users often have no option but to trust unregulated third party providers that sell and hold the currency, opening themselves up to fraud, loss and market abuse.

#### *Cyber-risks and data protection*

Consumers, investors and businesses using cryptocurrency platforms, wallets and exchanges are at risk from cyber-security threats such as hacking, ransomware and identity theft. It is also

not clear how operators can fully comply with data protection laws.

#### *Anonymity*

Due to the anonymous characteristics of cryptocurrencies, criminals can use them as a tool for tax evasion, theft, counterfeiting, money laundering and terrorist financing. While regulated entities must comply with anti-money laundering (AML) requirements, unregulated entities fall outside the scope of these laws and regulations. When transposed into Irish law, the EU's 5th Money Laundering Directive (AMLD5) will bring previously unregulated virtual asset service providers and online wallet providers within the scope of AML legislation. It will require them to put in place a risk-based AML framework and to conduct customer due diligence, monitor transactions and report suspicious activity.

### Status In Ireland

Ireland is a leading international finance centre that is home to an enviable mix of well-established financial services companies and a market-leading technology industry. This makes Ireland the perfect choice for firms exploring the evolving convergence of finance and technology in the area of digital money.

The Government of Ireland and the Irish financial services regulator, the Central Bank of Ireland (CBI), do not



currently guarantee or control the supply of any cryptocurrencies. The CBI does not view cryptocurrencies as money or legal tender, which means that there is no legal obligation for someone in Ireland to accept cryptocurrency as payment of a debt.

Despite this, there is no express prohibition on cryptocurrency related activities under Irish law.

## Application Of Existing Laws And Regulations

Broadly speaking, there is a lack of legal and regulatory certainty in Ireland on the application of existing laws and regulations to cryptocurrencies and crypto-assets.

Existing financial services regulations may apply to cryptocurrency trading platforms in areas like anti-money laundering when a form of transmission or money remittance is taking place, and to crypto-assets or tokens that are deemed to be ‘financial instruments’ or ‘transferable securities’ under MiFID II or ‘e-money’ under the E-Money Directive II (EMD2). However, many forms of cryptocurrencies and crypto-assets fall outside the scope of current regulatory frameworks that apply to electronic money, payment systems, and securities.

In terms of data privacy, regulators are grappling with the tension between the decentralised, permanent nature of a typical public cryptocurrency network and the high standards of protection the General Data Protection Regulation (GDPR) requires.

## What Is Happening In Ireland?

The CBI and various Irish government departments and state agencies have been actively considering cryptocurrencies and issuing their views on the important opportunities and material risks they present.

### CBI

The CBI has published warnings and alerts on the risks associated with buying and investing in cryptocurrencies and Initial Coin Offerings (ICOs) that aim to raise money from the public. The CBI’s view is that information disclosures to cryptocurrency and ICO participants tends to be incomplete, difficult to understand and does not fully relate the risks. The CBI also fed into the European Securities and Markets Authority’s

## “Technology-neutral regulation doesn’t need to spell the end of innovation.”

(ESMA) 2017 alert on the high risks of ICOs.

On the other hand, in light of a recent European Commission public consultation on creating an EU framework for markets in crypto-assets, the CBI has indicated that it is “supportive of this initiative and welcomes the development of a more harmonised approach to crypto-assets”. The CBI believes that the first step on clarity around the regulation of crypto-assets is aligning the terminology at an EU level, including harmonising the definition of a security token as a transferable security.

### Department of Finance

The Department of Finance’s 2018 white paper on cryptocurrencies and blockchain proposes that this area requires a collaborative approach across government agencies, as no one policy measure or group has the ability to comprehensively address all the risks and opportunities.

The Department has set up an inter-departmental working group on cryptocurrencies and blockchain that is closely monitoring innovations in the sector and reviewing risks and recommendations on cryptocurrency policy. The working group is engaging with Ireland’s consumer watchdog, the Competition and Consumer Protection Commission (CCPC), to draft guidance that updates the CCPC’s advice in relation to cryptocurrencies from 2018.

### Dáil Éireann

Ireland’s national parliament, the Dáil Éireann, published a research paper in 2020 on the regulatory challenges for cryptocurrencies. The paper notes that a suitable pan-EU or Irish regulatory regime would be welcome in this area as it would help protect consumers, defend monetary sovereignty and address criminal loopholes.

The Minister for Finance has answered a number of parliamentary questions on the government’s ‘wait and see’ approach

to cryptocurrencies, central bank digital currencies and ‘stablecoins’, a less volatile type of cryptocurrency often backed by government bonds and traditional currencies.

### Tax

The Revenue Commissioner issued updated guidance this year on the tax implications of profits from cryptocurrencies. This guidance confirms that, in general terms, there are no special tax rules in Ireland for cryptocurrencies and ordinary taxation principles apply to transactions involving cryptocurrencies.

## European Developments

As part of its Digital Finance Strategy, the European Commission recently issued a proposal for the regulation of crypto-assets. The proposed Regulation on Markets in Crypto-Assets (MiCA) will have a broad scope and create a legislative framework for all crypto-assets, including cryptocurrencies. It will apply to a range of entities including those issuing crypto-assets, firms providing crypto-assets services, and entities which enable consumers to buy and sell crypto-assets. If the proposal becomes law, crypto-asset service providers must have a physical presence in the EU and will require authorisation from their relevant national competent authority.

The proposed Regulation on Distributed Ledger Technology Market Infrastructures pilot regime aims to establish clear and uniform operating requirements for distributed ledger technology (DLT) market infrastructure. This pilot aims to reduce regulatory burdens on issuing and trading financial instruments in crypto-asset form.

## Global Coordination Efforts

Cryptocurrencies are becoming popular and external global factors such as the arrival of artificial intelligence, Brexit, and COVID-19 has accelerated their uptake.

Regulating decentralised, borderless and anonymous cryptocurrencies requires a coordinated pan-EU effort. Among other things, regulation needs to create reliable and predictable standards, protect consumers, investors and the economy, and restrict money laundering and terrorist financing. The International Monetary Fund (IMF) recently

called for formal global coordination on the regulation of cryptocurrencies. This desire for cross-border harmonisation has been echoed at an Irish and European level. The G7 and G20 intend to form a taskforce to look specifically at the topic of cryptocurrencies and stablecoins.

The regulatory objective at a European level is to create legal certainty for crypto-assets within the EU through a sound regulatory framework. The expansion of AML regulations to cryptocurrency providers and associated online wallet providers marks the first step towards the regulation of the provision and exchange of cryptocurrencies in Ireland. We expect to see the CBI and CCPC issue further guidance on cryptocurrencies and stablecoins over the coming months.

### Ireland Needs A Clear Cryptocurrency Plan

Cryptocurrency technology is rapidly evolving. That said, it is difficult to

directly regulate ‘a technology’ itself. Technology is the enabler - the better approach is to think in terms of regulating the operators and use cases. Increasingly, the intention of policymakers is therefore to try to propose laws and regulations that are technology-neutral.

Technology-neutral regulation doesn’t need to spell the end of innovation. It is possible to implement a fit for purpose regulatory framework for a cashless society that increases the efficiency of financial services, while protecting both citizens and the integrity of the financial system. To accomplish this, Ireland needs a clear plan and vision that avoids unintended consequences of diminishing consumer protection or security. Building trust will be a key factor. Regulatory sandboxes and innovation hubs can help test the technology in a safe and convenient environment. It is important that the Irish government is on board to help

drive the agenda at a European and global level.

When coming up with a regulatory framework for cryptocurrency and crypto-assets, policymakers need to adopt a balanced and proportionate approach to ensure there is a level playing field for operators and users. An onerous regulatory regime would almost certainly stifle innovation. As we have seen in other areas of financial technology, a collaborative approach to regulatory oversight involving all of the important stakeholders tends to be the most effective way to deliver real value and address the challenges and risks associated with innovative technologies. **IFC**

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