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AN ANALYSIS OF CRYPTOCURRENCY REGULATION WITHIN SOUTH AFRICA AND THE IMPACT THAT CRYPTOCURRENCY HAS ON EXISTING FINANCIAL REGULATIONS

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DECLARATION

I, Kyavand Gholizadeh Touchaei declare that:

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ABSTRACT

This research critically analyses a novel yet unknown area of law within South Africa — the regulation of cryptocurrencies. 'Cryptocurrency' refers to what is known as a Decentralised Convertible Virtual Currency (DCVC). In addition, cryptocurrency can be understood to be a subset of the collective term known as 'crypto asset'. Crypto assets encompass all cryptocurrencies, security tokens and utility tokens. It is often referred to as Financial Technology or Fintech.

The technology that underpins cryptocurrency is referred to as blockchain. Simply put, blockchain allows for information to be transacted between two points in a simple yet secure manner. This is done digitally through the use of the internet. In essence, a blockchain refers to information being stored in an encoded form on a peer-to-peer network. A blockchain may also be referred to as a ledger. Through a blockchain, a transaction is also more transparent, as it allows each party to the transaction to view all information relating to the blockchain. Blockchain technology can be applied to different aspects of various industries, such as contracts.

The basis of a cryptocurrency is to create a medium of exchange that is anonymous, secure, as well as relatively fast in terms of a transaction. However, one of the most important characteristics of a cryptocurrency is that it is unregulated. Through being unregulated, it allows cryptocurrencies to be used to circumvent financial regulations and engage in activities such as terrorism, money laundering and tax evasion. The reason for this is because cryptocurrencies are not linked to any central regulatory body, that can oversee cryptocurrency.

According to the South African Reserve Bank 2014 Position Paper, there are no express regulations for cryptocurrency in South Africa. Furthermore, cryptocurrencies are not recognised as legal tender in South Africa as they are not issued or controlled by a central regulatory body. Therefore, cryptocurrencies cannot be used as substitute as a legal tender. Through the 2014 Position Paper, risks were highlighted with regards to cryptocurrency transactions. However, no regulations were identified that could remedy these risks.

Following the 2014 Position Paper by SARB, SARB established the Intergovernmental Fintech Working Group (IFWG) and the Crypto Assets Regulatory Working Group (CARWG) in conjunction with the South African Revenue Service (SARS). Their goal is to review the position of cryptocurrency and consider any public policy in terms of cryptocurrency. In 2019, the IFWG and CARWG released a Consultation Paper, that further developed the understandings found in the 2014 Position Paper. Through the 2019 Consultation Paper, the

term crypto asset was adopted. As of April 2020, the IFWG, together with the CARWG released a Position Paper, which highlights various recommendations that can be used within South Africa in the general regulation of cryptocurrency, serving as the latest stance regulatory bodies have in relation to cryptocurrencies. Furthermore, the term crypto asset was also further developed and understood to be a collective term that includes cryptocurrencies as a subset.

It is also imperative to understand that many laws that apply to fiat currencies pre-dates the creation of cryptocurrencies. Therefore, many of these laws do not apply in regulating cryptocurrencies and will need further interpretation as well as amendment to be adapted in line with the concept of a cryptocurrency. Hence, by analysing the Twin Peaks model, and determining how cryptocurrencies interact with relevant laws found within the Prudential Authority and Financial Sector Conduct Authority, a greater understanding can be found as to how to regulate cryptocurrencies.

As it stands, the applicability of regulations is dependent on whether fiat currency is involved in a cryptocurrency transaction. If a cryptocurrency is being dealt with solely, the laws tend to falter due to the fact that South African regulators do not classify cryptocurrency as a legal tender.

Therefore, there is a possibility that users of cryptocurrency will be able to circumvent laws put into place to protect and preserve the financial sector of South Africa. The reason for this is that, many regulations within South Africa currently only apply to the definition of legal tender as mentioned by the SARB position paper of 2014.

Hence, in order for cryptocurrencies to be accepted within South Africa, there is a need for greater analysis of regulations, and in addition foreign countries such as the United Kingdom and the United States of America can be analysed. These countries provide a greater understanding as to how regulatory bodies can provide regulation for this novel technology within South Africa.

It can therefore be deduced, that through a greater understanding of this technology, there will be greater acceptance and better regulation of cryptocurrencies.

ABBREVIATIONS

AML/CTF	Anti-Money laundering/counter-terrorism financing
CARWG	Crypto Assets Regulatory Working Group
CASP	Crypto Asset Service Provider
CATM	Cryptocurrency Automated Teller Machine
CEA	Commodity Exchange Act 1936
CFTC	Commodities and Futures Trading Commission
COFI Bill	*Conduct of Financial Institutions Bill*
DCVC	Decentralised Convertible Virtual Currency
E-money	Electronic Money
EU	European Union
FAIS	Financial Advisory and Intermediary Services Act 37 of 2002
FATF	Financial Action Task Force
FCA	Financial Conduct Authority
FIC	Financial Intelligence Centre
FICA	Financial Intelligence Centre Act 38 of 2001
FinCEN	Financial Crimes Enforcement Network
Fintech	Financial Technology
FinSurv	Financial Surveillance Department of the Bank
FMA	Financial Markets Act 19 of 2012
FSCA	Financial Sector Conduct Authority
FSP	Financial Service Provider
FSRA	Financial Services Regulations Act 9 of 2017
HMRC	HM Revenue and Customs
ICO	Initial Coin Offerings
IFWG	Intergovernmental Fintech Working Group
IRS	Internal Revenue Service
KYC	Know-Your-Customer
MLR	Money Laundering, and Terrorist Financing and Transfer of Funds Regulations 2017
NPRM	Notice of Proposed Rule Making
NPS Act	National Payment System Act 78 of 1998
NPSD	National Payment System Department
OSS	Open-source Software

P2P	Peer-to-Peer Network
PA	Prudential Authority
PoS	Proof-of-Stake
PoW	Proof-of-Work
SARB	South African Reserve Bank
SARB Act	South African Reserve Bank Act 90 of 1989
SARS	South African Revenue Services
SDA	Single Discretionary Allowance
SEC	Securities and Exchange Commission
UK	United Kingdom
USA	United States of America
USD	United States Dollar

CHAPTER 1

INTRODUCTION & OVERVIEW

I. BACKGROUND

Cryptocurrency[1] is a novel concept that is growing in popularity within South Africa as well as around the world. Traditionally, the global economy was centralised around fiat currencies,[2] with the most important of these currencies being the United States Dollar (USD).[3] In recent years, the USD has been subjected to many influences that have resulted in a ripple effect to various economies around the world. An example of this is the financial crisis of 2008, which gave rise to a global recession.[4]

However, in comparison to fiat currency, cryptocurrency is independent of the overall state of the economy and is not impacted by typical market movements that may occur. This can be attributed to the fact that cryptocurrency is decentralised and therefore unregulated.[5]

With the COVID-19 outbreak,[6] it has resulted in a stalling of the traditional economy, with devastating consequences forecasted towards economic growth. Furthermore, within South Africa, the effects of the COVID-19 have been noticed with the weakening Rand. By virtue of cryptocurrency being decentralised, it should not (in theory) have been affected by this global economic downturn.[7] However, when the economy started to slump, investors relied on fiat currency as opposed to cryptocurrency, resulting in the value of cryptocurrency to also fall and therefore, be affected by the COVID-19 outbreak, causing a volatility in the price of crypto assets. It must be noted that cryptocurrency lacks formal adoption and it is seen as an asset rather than an

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[1] A cryptocurrency is best defined as being a decentralised convertible virtual currency. Cryptocurrencies are based on an open source, peer-to-peer system. It is seen as being decentralised as there is no central administering authority over cryptocurrency. Furthermore, cryptocurrency is maths based and generated through encryption techniques. A Niemand 'A Few South African Cents' Worth on Bitcoin' (2015) 18 *PER* at 1979-2010.

[2] Fiat currencies refers to money (such as paper currency) not convertible into coin or specie of equivalent value. 'Fiat Currency' Merriam-Webster, available at: *https://www.merriam-webster.com/dictionary/fiat%20mone,* accessed on: 21 march 2020.

[3] 'Impact of Cryptocurrency in the Growth of Economy', *Evonax* 2019, available at: *https://www.evonax.com/blog/2019/06/14/impact-of-cryptocurrency-in-the-growth-of-economy.html*, accessed on: 5 March 2020.

[4] 'How Cryptocurrency is Disrupting the Global Economy', *Medium* 2018, available at: *https://medium.com/the-mission/how-cryptocurrency-is-disrupting-the-global-economy-89347581aa93*, accessed on: 14 March 2020.

[5] U Chohan, 'The Coronavirus Lesson: Do Cryptocurrencies offer a counter-cyclical hedge?', *SSRN* 2020, available at: *https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3566265*, accessed on: 8 April 2020.

[6] The coronavirus disease 2019 (COVID-19) was first reported on 31 December 2019 by the World Health Organisation country office following a cluster of pneumonia cases in Wuhan City, Hubei Province of China, and eventually spread to the rest of world, being declared a global pandemic baby the World Health Organisation; The causative virus has been identified as a severe acute respiratory syndrome coronavirus 2 (SARS-CoV-2). The result of this virus is that through closures of cities as well as countries borders, it has impacted the global economy negatively. 'Covid-19 Background', *National Institute for Communicable Diseases* 2020, available at: *https://www.nicd.ac.za/diseases-a-z-index/covid-19/*, accessed on: 12 April 2020.

[7] U Chohan, 'The Coronavirus Lesson: Do Cryptocurrencies offer a counter-cyclical hedge?' op cit note 5.

alternate currency. It is yet to be seen whether, with greater adoption, there may be less influence to the general value of cryptocurrency based on economic events that may occur in the future.[8]

a) Foundation and concept of cryptocurrency

Cryptocurrency refers to what is known as a Decentralised Convertible Virtual Currency (DCVC).[9] Cryptocurrency, furthermore, influences the financial market through technology, and according to the International Monetary Fund (IMF), is often referred to as Financial Technology or Fintech.[10]

The technology that underpins these virtual currencies are referred to as blockchain. Simply put, blockchain[11] allows for information to be transacted between two points in a simple yet secure manner. This is done digitally through the use of the internet.[12] In essence, a blockchain refers to information being stored in an encoded form on a peer-to-peer network (P2P network). A blockchain may also be referred to as a ledger. Through a blockchain or ledger, a transaction is also more transparent when compared to conventional transactions. A blockchain allows each party to the transaction to view all information relating to the blockchain. This allows each party to protect their respective interests, as well as introduce fast transactions and eliminate the need for third parties to oversee the transaction.

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[8] M Orkutt, 'Coronavirus is forcing fans of Bitcoin to realize it's not a "safe haven" after all', *MIT Technology Review* 2019, available at: *https://www.technologyreview.com/2020/03/19/905207/coronavirus-is-forcing-fans-of-bitcoin-to-realize-its-not-a-safe-haven-after-all/,* accessed on: 8 April 2020.

[9] DCVC refers to an open source, peer-to-peer system, that relies on algorithms as well as cryptography for its existence. DCVC's are also not regulated by any authorities. By virtue of being a DCVC, this means that cryptocurrency, is a subset of virtual currencies. There are various examples of DCVC's, with the leading example being Bitcoin. E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' (2019) 31 *SA Mercantile Law Journal* at 1-28.

[10] Financial Technology refers to traditional financial services that are integrated with technology. Fintech is often seen as a disruptive technology that is used by businesses as it ushers a new way to do business; I Chiu 'Fintech and Disruptive Business Models in Financial Products, Intermediation and Markets Policy Implications for Financial Regulators' (2016) 21 *Journal of Technology Law and Policy* 55 at 58.

[11] A blockchain occurs when a transaction between 2 individuals is requested. This particular request is then sent to many computers, which are all part of the same network. This particular network is known as a peer-to-peer (P2P) network. The transaction is then validated by 'miners'. Once the transaction is validated, the transaction becomes a 'block'. This 'block' contains all the particular transaction details of the sender and receiver. The new block is then added onto existing blocks, sequentially. This therefore then creates a chain of blocks, hence the name blockchain. Falsifying a blockchain is near impossible, as falsifying a single block would mean falsifying the entire blockchain. T Simba 'Blockchain Explained' (2019) 8 *HR Future* 34; See also: A Rosic, '17 Blockchain Applications That Are Transforming Society', *Block Geeks* 2017, available at: *https://blockgeeks.com/guides/blockchain-applications/#comments*, accessed on: 25 February 2020; 'How does a blockchain work?', *Bitpanda Academy*, available at: *https://www.bitpanda.com/academy/en/lessons/how-does-a-blockchain-work/*, accessed on: 26 February 2020; A Rosic, 'What is Blockchain Technology? A Step-by-Step Guide for Beginners', *Block Geeks* 2015*,* available at: *https://blockgeeks.com/guides/what-is-blockchain-technology/* , accessed on: 25 February 2020.

[12] E Reddy & V Lawsack, op cit note 9.

Blockchain also consists of a 'public' blockchain that contains every transaction processed, which allows the computers found within the P2P network to verify the validity of each transaction, further adding to the overall security and transparency of a blockchain.[13] Blockchain technology does not only apply to the use of virtual currencies, but can be applied to different aspects of various industries.[14]

In 2009, Satoshi Nakamoto (a pseudonym) created a type of cryptocurrency known as Bitcoin, and authored the Bitcoin White Paper.[15] The basis of Bitcoin is to create a medium of exchange that is anonymous, secure as well as relatively fast in terms of a transaction.[16] However, the main feature of Bitcoin is that it is an unregulated medium of exchange.[17]

Hence, no country in the world has the power to regulate or control the distribution of Bitcoin. This gives Bitcoins a stark difference to traditional Fiat currencies of the world. Bitcoins fall within an umbrella of various cryptocurrencies.[18] Out of all cryptocurrencies, Bitcoin is seen as being the leader as well as most popular cryptocurrency currently in use.[19]

b) Regulation of cryptocurrency

The possession as well as exchange of bitcoin are seen to be appealing to many users due to the fact that they remain largely unregulated within South Africa. Hence, cryptocurrency is seen to have a value that can be exchanged to an equivalent value in fiat currency. In addition, cryptocurrencies have reduced costs and transactional speeds, as well as no intermediaries involved in the transaction. However, through being unregulated, it allows Bitcoin, as well as

[13] A Rosic, '17 Blockchain Applications That Are Transforming Society' op cit note 11.
[14] The most common application can come in the form of a smart contract. Through a blockchain the smart contract can be programmed to self-execute and self-maintain, once all terms of the contract have been met. For a smart contract, normally an intermediary ensures all parties follow through on the terms of a conventional contract. However, blockchains waves the need for third parties and ensures that all blockchain participants know the contract details and that contractual terms are implemented automatically once conditions are met. Blockchain can also be applied to musicians. Music, especially digital music face major issues regarding piracy, ownership as well as royalties paid to musicians. Through the use of blockchain and smart contracts, a database of music rights can be created and furthermore through blockchain it will allow for a transparent transaction of royalties as well as real time distribution of music by relying on the technology. There are many other applications of blockchain, such as to smart property, healthcare and appliances; A Rosic, '17 Blockchain Applications That Are Transforming Society' op cit note 11.
[15] The Bitcoin White Paper gives in-depth information about the technology as well as background required to understand what bitcoin is and how it operates in relation to cryptocurrency.
[16] A Niemand 'A Few South African Cents' Worth on Bitcoin' op cit note 1.
[17] Ibid.
[18] 'How Cryptocurrency is Disrupting the Global Economy', op cit note 4.
[19] Ibid.

other cryptocurrencies to be used to circumvent financial regulations and engage in activities such as terrorism, money laundering and tax evasion.[20]

According to the *Position Paper on Virtual Currencies* (hereinafter referred to as the 2014 Position Paper),[21] there are no express regulations for cryptocurrency in South Africa. This position paper merely highlighted the risks[22] people would face should they proceed to use or deal in cryptocurrency.[23] The 2014 Position Paper furthermore, classified cryptocurrency. According to this position paper, cryptocurrency does not fall within the classification of a fiat currency/legal tender[24] in South Africa. Therefore, cryptocurrency cannot be used as a substitute for legal tender, as payment of an obligation.[25]

In addition, the 2014 Position Paper does not consider cryptocurrency as being electronic money(e-money), or a security.[26] Being aware of the definitions and classification of cryptocurrency is crucial. It allows for interpretation of existing regulations and to see whether these regulations are applicable to cryptocurrency.

Following the 2014 Position Paper, the South African Reserve Bank (SARB) established the Intergovernmental Fintech Working Group in 2016 (IFWG). The IFWG aims to develop an understanding among policy makers and regulators, in order to understand the implications that cryptocurrencies have for the financial sector and economy. Furthermore, the Crypto Assets Regulatory Working Group (CARWG) was established in conjunction with the IFWG and South African Revenue Service (SARS) in 2018. Their goal is to review the positions of cryptocurrency and consider any public policy in terms of cryptocurrencies.[27]

In 2019, the IFWG and CARWG released a consultation paper entitled *The Consultation Paper on Policy Proposals for Crypto Assets*, which was published in 2019 (hereinafter referred to as the 2019 Consultation Paper).

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[20] South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* (2014).

[21] Ibid.

[22] The particular risks that were identified by the position paper include money laundering, fraud, funding of terrorism as well as hacking; Ibid.

[23] Ibid.

[24] The 2014 position paper highlighted that the SARB is only permitted to issue legal tender, which includes bank notes and coins of South Africa. It is this legal tender that can be offered as a payment for an obligation; Ibid.

[25] As authorised by s 14 of the South African Reserve Bank Act 90 of 1989 and the National Payment Systems Act 78 of 1998; See also: South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* op cit note 20 at 4-5.

[26] The view of the 2014 SARB position paper is that electronic money would only be valid if the money is provided by a bank, or if the merchant has an agreement with the bank. E Reddy & V Lawack op cit note 9.

[27] Within the 2019 Consultation Paper it highlighted various areas of concern relating to cryptocurrency, which included: Purchasing/selling, payments, capital raising through initial offering, cryptocurrency derivatives, market provision. However, the CARWG primarily focuses on the purchasing/selling and payments of cryptocurrency within South Africa. Intergovernmental Fintech Working Group, Crypto Assets Regulatory Working Group *Consultation Paper on Policy Proposals for Crypto Assets* (2019).

Through the 2019 Consultation Paper, the definition of cryptocurrency was further evolved, and it was determined that a cryptocurrency forms a category within the collective class name known as 'crypto asset'. Furthermore, the 2019 Consultation Paper's focus was emphasised on the development of regulatory proposals. This contrasts the 2014 Position Paper which provided an understanding to the risks and technology underpinning cryptocurrencies. In addition, this consultation paper identified the potential uses that cryptocurrencies may be utilised for and also the manner in which South Africa can adopt to promote the anti-money laundering/counter terrorism financing (AML/CTF) recommendations as proposed by the Financial Action Task Force (FATF),[28] through the use of cryptocurrencies.[29]

In 2020, the IFWG and CARWG published the *2020 IFWG CARWG Position Paper* (hereinafter referred to as the 2020 Position Paper). The 2020 Position Paper further built on the knowledge of the past papers and made thirty recommendations that addressed the risks highlighted in the 2014 Position Paper. Furthermore, the 2020 Position Paper expanded on the findings presented in the 2019 Consultation Paper, by providing recommendations, as to how cryptocurrency may be regulated. In addition to these recommendations, the Position Paper further addressed the definition of a cryptocurrency.

Through these policy papers, it can also be understood that a cryptocurrency does not represent money or legal tender, but may perform similar functions to security, currency and commodities. Furthermore, through these papers, it emphasises the importance of understanding the definition and classification of cryptocurrency, namely, that it is a 'crypto asset' rather than a 'currency' when interpreting laws. [30]

It is important to, however, understand that these policy papers merely represent the stance employed by the involved regulatory bodies on how cryptocurrencies should be treated. These policy papers are not law.

Hence, it is also imperative to understand that many laws that apply to fiat currencies pre-date the creation of cryptocurrencies. Therefore, these laws do not apply in regulating cryptocurrencies and will need further interpretation as well as amendments to be adapted in line with the concept of a cryptocurrency. This can be achieved by analysing the policy papers and

[28] The FATF is an inter-governmental body involved with setting international standards that prevent money laundering and the financing of terrorism. Recommendations for the FATF can be found at: *http://www.fatfgafi.org/publications/fatfrecommendations/documents/regulation-virtual-assets.html.*
[29] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group *Consultation Paper* op cit note 27.
[30] Ibid.

observing if amendments can be made in relation to existing legislation to regulate cryptocurrencies.

Hence relevant Prudential Authority regulations such as the SARB Act 90 of 1989 and the Banks Act 94 of 1990 must be examined in relation to cryptocurrency. In addition, cryptocurrency must also be analysed in relation to relevant Financial Sector Conduct Authority regulations, which include: Financial Intelligence Centre Act 38 of 2001, Financial Advisory and Intermediary Services Act 37 of 2002, Financial Markets Act 13 of 2012, and the Financial Services Regulation Act 9 of 2017 must be examined in relation to cryptocurrency.[31] The reason for this analysis is to determine whether relevant prudential and market regulation will be applicable in the regulation of cryptocurrencies.

In keeping with the financial sector, but looking further into border restrictions and regulations, the Currency and Exchanges Act 9 of 1933 must be considered and interpreted to determine if any amendments must be made, to apply to the use of cryptocurrency. This particular Act (in relation to fiat currency) is concerned with the movement of funds in and out of South Africa to off-shore accounts.[32]

As a result of a cryptocurrency's unregulated nature, it has also piqued the interest of international financial regulators. There is no consistent regulation of cryptocurrency, with different countries adopting differing approaches with regards to cryptocurrency. Various countries have touched on the known concerns associated with cryptocurrencies, and these international regulatory approaches can be used to draw a comparison to the South African regulatory approach. Countries such as the United States of America and The United Kingdom can be used as a comparison in developing more stringent regulations for South Africa. The reason this comparison can be made, is because South Africa's international counterparts have a more developed legal framework that regulates the use as well as exchange of cryptocurrency within their respective jurisdiction.

c) Impact of cryptocurrency on existing financial regulations of South Africa

In order to determine the impact cryptocurrency has on existing financial regulations within South Africa, an analysis of the policy papers will be required. These policy papers include the 2014 Position Paper, the 2019 Consultation Paper and the 2020 Position Paper. Through an analysis of

[31] A Itzikowitz & I Meiring, 'Blockchain and Cryptocurrency Regulation 2020 South Africa', *Global Legal Insights* 2020, available at: *https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/south-africa,* accessed on: 12 April 2020.
[32] Ibid.

these policy papers, recommendations and suggestions on amendments to be made to include cryptocurrency within a regulatory framework can be determined. The amendment and interpretation of laws within the financial sector will need to be done in a manner that understands the definition and classification of cryptocurrency in relation to fiat currency.

By looking at certain regulations such as the Financial Intelligence Centre Act 38 of 2001 (FICA), it requires cryptocurrency service providers to employ the use of Know-Your-Customer[33] protocols. This allows for identification of users of cryptocurrency through their service providers respectively. However, this regulation only applies to cryptocurrency service providers established within the borders of South Africa.[34]

Hence, this form of regulation does not take into account cryptocurrency service providers that originate out of South Africa. Furthermore, by looking at the FICA in general, it also only applies to legal tender in the form of money and does not apply to cryptocurrency in any way, as cryptocurrency does not constitute as legal tender in South Africa.

Hence, the FICA will only apply if there is an exchange between legal tender used to buy cryptocurrency at a service provider registered in South Africa. Therefore, if cryptocurrency is exchanged for another type of cryptocurrency, or if the service provider originates overseas, it will allow users to circumvent money laundering laws as FICA will not apply. [35]

Furthermore, when considering offshore accounts, generally it is regulated by the Currency and Exchanges Act 9 of 1933. This Act does make provision for any person wishing to exchange offshore fiat currency funds for the purpose of buying cryptocurrency. However, when dealing with offshore cryptocurrency accounts, the Act remains silent and is not regulated.[36]
There are many more examples of this 'part regulation' of cryptocurrencies within South Africa that will be further explored in this research paper. But the key aspect to understand with regards to regulations within the financial sector, is that the applicability of these regulations is dependent on whether a fiat currency is involved in the transaction. If a cryptocurrency is being dealt with

[33] This protocol is found within financial services and requires that financial institutes and service providers are aware of the identity of customers. This will allow to monitor transactions of customers to prevent money laundering. Know-Your-Customer is primarily made up of four elements:
- Customer acceptance policy
- Customer identification procedures
- Monitoring of transactions/ongoing due diligence
- Risk management

[34] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies 'op cit note 9.
[35] A Itzikowitz & I Meiring, op cit note 31.
[36] Currency and Exchanges Act 9 of 1933; See also: A Itzikowitz & I Meiring, op cit note 31.

exclusively, the laws tend to falter due to the fact that South African regulators do not classify cryptocurrency as a legal tender.

Hence the impact that cryptocurrency may have, is that existing regulations may create a high possibility that users of cryptocurrency will be able to circumvent laws put into place to protect and preserve the financial sector of South Africa. The reason for this is that, many regulations within South Africa currently only apply to regulating legal tender, and cryptocurrencies do not fall within the ambit of a legal tender.

Therefore, in order for cryptocurrencies to be accepted within South Africa, confidence in and support of cryptocurrencies needs to be built. This will only happen if there is greater analysis of regulations and the determination of the impact that cryptocurrency has on these regulations. Furthermore, there needs to be an interpretation of the concept of cryptocurrency, to determine if it brings the concept of cryptocurrency closer or in line with the meaning of a legal tender as envisaged by SARB, hence allowing many financial laws to apply to it, or alternatively, whether an amendment of the laws would have to be conducted in order for the laws to be in line with the dynamic nature and concept of cryptocurrency.

II. STATEMENT OF PURPOSE

The purpose of this dissertation is to provide an analysis on regulations of cryptocurrencies found within South Africa. These South African regulations would then be compared and contrasted against foreign jurisdiction regulations to determine if any further learning or recommendations can be determined and supplemented to the South African regulations of cryptocurrencies. A further analysis will be conducted to determine the impact cryptocurrency has on existing South African regulations. Lastly recommendations to current regulations will be suggested.

III. RATIONALE

Through the introduction of cryptocurrency as well as advancements in financial technology, it has resulted in fiat currencies being challenged by cryptocurrencies as a medium of exchange.

Although it has helped to forge an alternate method of payment, it has also brought about various risks that threaten the financial sector of South Africa. Many countries have highlighted risks such as money laundering and terrorism laws that can be circumvented by cryptocurrency.

It is therefore essential that cryptocurrencies are assessed against the South African framework and that regulations and laws are made for the purposes of regulating cryptocurrency.

Due to the fact that cryptocurrency is a relatively new technology within South Africa and is a dynamic concept, there is very little legislation pertaining to cryptocurrency. Legislation that

applies to cryptocurrency are those that have been merely adapted but are vague in terms of the covering cryptocurrency.

There is a wide range of scholarly articles relating to the topic of cryptocurrency, however these articles merely provide and overall understanding of the concept of cryptocurrency and do not go in-depth into the development of laws that is exclusive to cryptocurrency as well as the general impact cryptocurrency.

This dissertation will therefore aim to contribute to the topic of cryptocurrency by offering recommendations on regulating cryptocurrency within South Africa and the general impact cryptocurrency has on existing financial regulations.

IV. RESEARCH QUESTIONS

The main question of this dissertation is looking at an analysis of cryptocurrency regulation within South Africa and the impact that cryptocurrency has on existing financial regulations. To answer this main question, the following sub-questions will be considered:

A. What is cryptocurrency?
B. How does cryptocurrency impact relevant financial regulations within South Africa?
C. How is cryptocurrency currently regulated in South Africa?
D. What lessons can be learned from international jurisdictions such as the United Kingdom and the United States of America, on cryptocurrency?
E. What recommendations may be offered to regulate cryptocurrencies within South Africa?

V. RESEARCH METHODOLOGY

A desktop research methodology is this study's primary research approach. The reason this research approach will be relied on is because it includes a review and analysis of any laws, case law and literature in respect to cryptocurrency, bitcoin and the global market. The desktop study will aim to answer the research questions by gathering and analysing sources that exist and are available in print or electronic format.

The internet will primarily be utilised to aid this research. A collection of primary and secondary sources using electronic search engines such as Juta, LexisNexis, Google Scholar and Sabinet will be used. In addition to electronic search engines, due to the fact that cryptocurrency is a relatively new topic and that scholarly articles and legislation is scarce, online news articles as well as online websites would be relied upon to gather information.

In terms of the primary sources, the 2014 Position Paper, 2019 Consultation Paper, as well as the 2020 Position paper will be primarily relied on. Other primary sources that would be used, include South African legislation and case law where applicable.

International law will also be relied upon to further emphasise and substantiate points not covered by South African law.

Secondary sources such as academic literature, journals, online academic research paper, websites and online news articles will further be used to determine the strengths and weaknesses of cryptocurrency and emphasise recommendations of this dissertation.

In addition, this dissertation will also contain comparative research in terms of which cryptocurrency laws in South Africa are compared to foreign law. This is required due to the fact that cryptocurrency is a relatively novel concept in South Africa, and through this comparison it would allow recommendations to be drawn from foreign jurisdictions, for this dissertation.[37]

VI. STRUCTURE OF RESEARCH PROJECT

This research project will consist of six chapters.

Chapter 1 provides an overview and introduction to the topic of cryptocurrency. It describes the purpose of the study, the research questions and the research methodology to be applied when answering the research questions.

Chapter 2 provides an analysis into the basic concept of cryptocurrency. Within this chapter the history of cryptocurrency, in particular Bitcoin will be explored. The technology underpinning cryptocurrency as well as the general technical facilitation of cryptocurrency will be explained. Furthermore, an analysis into the definition of cryptocurrency will be conducted.

Chapter 3 will provide an in-depth analysis into the published policy papers, namely the 2014 Position Paper, 2019 Consultation paper and 2020 Position Paper. Through the analysis of these policy papers, the impact of cryptocurrency on financial regulations can be determined, and the recommendations on the regulation of cryptocurrency further analysed.

Chapter 4 will provide an in-depth analysis into the laws and regulations of South Africa pertaining to cryptocurrency.

Chapter 5 provides an analysis of foreign law and a comparative study between South African regulations and foreign counterparts will be conducted. Lessons that can be drawn from foreign jurisdictions will also be stated.

[37] All research contained within this dissertation is correct up to the date of 01 April 2021.

Chapter 6 will serve to make recommendations on how to regulate cryptocurrencies within South Africa and will set out the conclusions and summarise the recommendations for a way forward within the topic of cryptocurrency.

CHAPTER 2

THE BASIC CONCEPTS RELATING TO CRYPTOCURRENCIES

I. CHAPTER OVERVIEW

This chapter will provide an in-depth analysis into the concept of cryptocurrency within South Africa. Through this chapter, an overview of cryptocurrency will be discussed, which will look at the general definition of cryptocurrency and its classifications within financial technology. Furthermore, an in-depth discussion will be conducted on the various types of cryptocurrencies. In addition, the technology known as blockchain, which underpins cryptocurrency will be analysed in order to provide a broader understanding in relation to the operation of cryptocurrency. Lastly, from a practical standpoint, the methods to obtain and store cryptocurrencies will be explored.

II. OVERVIEW OF CRYPTOCURRENCY

a) Definition

According to the South African Reserve bank (SARB), through the 2014 Position Paper, a cryptocurrency is classified as being a decentralised convertible virtual currency (DCVC).[1]

In understanding the concept of DCVC's, SARB contrasted this concept with other forms of virtual currencies available, most notably, convertible virtual currencies, non-convertible virtual currencies, as well as electronic money (e-money).[2]

According to the 2014 Position Paper, a decentralised convertible virtual currency (DCVC) refers to cryptocurrencies, and a well-known example of a DCVC includes Bitcoin.[3] In order to understand cryptocurrencies, it is important to understand the concept of a DCVC.

In terms of being decentralised, this means that cryptocurrencies operate without any central body or controlling institution, hence there are no regulations or particular oversight over the use of cryptocurrencies by any central or reserve banks of a country.[4] Instead, a cryptocurrency maintains itself through an internal protocol framework that is maintained by crypto-miners.[5] Furthermore, by virtue of being decentralised it means that transactions can occur freely without the need for permission from financial/regulatory bodies.[6]

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[1] South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* (2014) at 2-5.
[2] Ibid.
[3] South African Reserve Bank National Payment System Department op cit note 1 at 2-3.
[4] South African Reserve Bank National Payment System Department op cit note 1 at 2.1.
[5] S Hughs & S Middlebrook 'Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries '(2015) 32 *Yale Journal on Regulation* 495.
[6] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' (2019) 31 *SA Mercantile Law Journal* at 1-28.

In terms of being convertible, this merely refers to the fact that cryptocurrencies can be exchanged for fiat currencies and vice versa.[7] The SARB views virtual currencies as being: 'digital representation of value that can be digitally traded and functions as a medium of exchange, a unit of account and/or a store of value but does not have legal tender status.'[8]

Through the 2014 Position Paper, it was found that the term 'virtual currency', as found within the acronym of 'DCVC', departs from what is considered as a traditional means of banking.[9] Furthermore, although a virtual currency contains the term 'currency' within its termed name 'virtual currency', it must not be confused with the features of a traditional fiat currency/legal tender. Legal tender refers to coins or notes that are issued by a bank.[10]

Hence, a virtual currency, in the eyes of SARB is not seen as legal tender, and therefore not currency. However, it does share certain characteristics with fiat currency/legal tender, such as being a medium of exchange and its ability to store value. This understanding therefore affects a virtual currency's legal validity in so far as being categorised as 'legal tender'.[11]

Virtual currencies therefore, refer to a medium of exchange that is intangible and exists digitally.[12] Although a virtual currency is not considered as being a legal tender, it is perceived as being a substitute for legal tender.[13] Within virtual currencies, there are various categories,[14] with cryptocurrencies forming one of these categories.[15]

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[7] South African Reserve Bank National Payment System Department op cit note 1 at 2.

[8] Ibid; See also: Financial Action Task Force: FATF Report *Virtual currencies key definitions and potential AML/CFT risks* (2014).

[9] In a basic sense, traditional banking refers to operational branches of financial institutions that offer financial services and administrative services to their respective clients. Traditional banks also offer the use of automated teller machines for their customers. Furthermore, traditional banks provide a focus on face-to-face customer services. However, through evolving technology as well as the need to be connected, traditional banking had to evolve beyond face-to-face customer services, resulting in digital banking being introduced. Digital banking consists of online as well as mobile banking, which eliminates the need for face-to-face customer services, but still preserves the need for a bank to facilitate a transaction. Furthermore, traditional banking refers to institutions facilitating transactions concerning legal tender as defined by the South African Reserve Bank. Through the use of Fintech, it has resulted in the need for traditional banking systems to further evolve. This is due to the fact that Fintech departs from traditional banking systems in this sense that it is decentralised, meaning that it is not regulated by any legislation or controlled in any way by any institution or individual, hence removing the 'middle-man' (banking institutions) from transactions between relevant parties. This in turn, makes crypto asset transactions easier, simpler and cheaper, than traditional banking transactions. Therefore, to overcome such a challenge and to remain competitive, traditional banks would need to further evolve their offered services, towards a more customer-centric based model. 'The differences between traditional and online banking' *Expatica* 2020, available at: *https://www.expatica.com/be/finance/banking/the-differences-between-traditional-and-online-banking-1299954/*, accessed on: 22 July 2020; See also: J Klostermann 'Fintech and blockchain vs. traditional banking' *Fintech News* 2020, available at: *https://www.fintechnews.org/fintech-and-blockchain-vs-traditional-banking/,* accessed on 22 July 2020; South African Reserve Bank National Payment System Department op cit note 1 at 2-5.

[10] Section 3.2.4 of the South African Reserve Bank Act 90 of 1989.

[11] South African Reserve Bank National Payment System Department op cit note 1 at 2.

[12] Ibid.

[13] S Hughs & S Middlebrook 'Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries' op cit note 5.

[14] These categories include virtual currencies such as e-money, which is distinguished from crypto assets.

[15] S Hughs & S Middlebrook 'Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries' op cit note 5.

Contrasting a DCVC, a convertible virtual currency refers to a virtual currency that can be exchanged between virtual currency and legal tender, and vice-versa. It may be centralised or decentralised. A centralised convertible virtual currency is associated with a particular administrating authority that controls the way the virtual currency is used, redeemed and issued.[16] An example of a centralised convertible virtual currency is the Linden Dollar.[17]

On the other hand, non-convertible virtual currencies are all centralised and refer to virtual currencies that cannot be exchanged for legal tender. By virtue of being centralised, it means that the virtual currencies are under a single authority of a particular group or virtual community. An example of a non-convertible virtual currency includes 'gold' that can be purchased using legal tender, from Clash Royale, a popular multiplayer online game.[18]

Hence, it can be noted that non-convertible virtual currencies are therefore traditionally used and associated within online or virtual platforms. This type of virtual currency does not store value or increase wealth.[19] However, in comparison, a DCVC can be used as a medium of exchange that is a store of value, can be used to trade/speculate and is an alternative to traditional legal tender.

In establishing that a cryptocurrency is considered as being a DCVC, the 2014 Position Paper had to determine whether a cryptocurrency can be considered as a form of 'currency' or 'legal tender'. SARB relied on its findings that a 'virtual currency' such as a DCVC does not constitute as a form of legal tender.[20] In applying this logic towards the concept of a cryptocurrency the 2014 Position Paper does not view cryptocurrency as fitting the definition of a legal tender.[21]

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[16] South African Reserve Bank National Payment System Department op cit note 1 at 2-3; See also: A Niemand 'A Few South African Cents' Worth on Bitcoin' (2015) 18 PER at 1979-2010.

[17] Linden Dollar is a convertible virtual currency that can be purchased through the exchange of the United States Dollar. Linden Dollar is a virtual currency that is used within the online programme known as Second Life, that allows users of the program to have an online alternate virtual life, where they can use Linden Dollars to purchase, rent or trade for virtual goods and services that are found within the Second Life programme. The Linden Dollar can be exchanged between a convertible virtual currency and a legal tender and vice-versa. G Scott 'Linden Dollar' *Investopedia* 2019, available at: *https://www.investopedia.com/terms/l/linden-dollar.asp*, accessed on: 3 July 2020.

[18] This 'gold' can be used to purchase particular perks within the game that can be utilised by the respective player. However, the 'gold', once purchased using legal tender, cannot be exchanged for an equivalent value in legal tender. South African Reserve Bank National Payment System Department op cit note 1 at 2-3; See also: A Niemand 'A Few South African Cents' Worth on Bitcoin' op cit note 16.

[19] This type of virtual currency typically is only used for entertainment purposes and can be seen as being analogous to 'old-school' video game arcade coins.

[20]South African Reserve Bank National Payment System Department op cit note 1 at 4-5.

[21] 'Only the Bank (South African Reserve Bank) is allowed to issue legal tender i.e., bank notes and coins in (the Republic of South Africa) RSA which can be legally offered in payment of an obligation and that a creditor is obliged to accept. Therefore, (decentralised virtual currencies such as cryptocurrencies) DCVCs are not legal tender in [the Republic of South Africa] RSA and should not be used as payment for the discharge of any obligation in a manner that suggests they are a perfect substitute of legal tender.' Hence this quote illustrates that cryptocurrencies are not legal tender. South African Reserve Bank National Payment System Department op cit note 1 at 4-5. As authorised by Section 14 of the South African Reserve Bank Act 90 of 1989 and the National Payment Systems Act 78 of 1998; See also: A Nieman 'A Few South African Cents' Worth on Bitcoin' op cit note 16.

Furthermore, it must be noted that the concept of 'currency' refers to legal tender that is issued by the Reserve Bank. Hence by virtue of a cryptocurrency being unregulated as well as a virtual currency, it does not fall under the classification of a currency.[22]

In determining that a cryptocurrency cannot be considered as a legal tender, the 2014 Position Paper went further to contrast cryptocurrencies in relation to electronic money (e-money). According to the 2014 Position paper, e-money is defined as:

> …electronically stored monetary value issued on receipt of funds and represented by a claim on the issuer. E-money is generally accepted as a means of payment by persons other than the issuer and is redeemable for physical cash or a deposit into a bank account on demand.[23]

Furthermore, e-money is seen as forming part of the bank's business in terms of the Banks Act No.94 of 1990. Hence, e-money may be deposited into a bank account or redeemed for legal tender. Contrasting e-money, DCVC's may only be utilised as a medium of exchange from legal tender to DCVC and vice versa. A DCVC cannot be deposited into a bank account, and therefore does not form part of a bank's business.[24]

In making these conclusions, the 2014 Position Paper also referred to the National Payment System Department's (NPSD) 2009 position paper regarding e-money. The 2014 Position Paper relied on this NPSD position paper to further determine if cryptocurrency can fall within the e-money classification, and it was determined that cryptocurrency cannot be classified as e-money.[25]

According to NSPD position paper on e-money, it was found that e-money 'can only function legally if they are provided by a bank, or if the merchant/company that offers the product enters into a partnership agreement with a bank.'[26]

Therefore, by noting the fact that cryptocurrency is not a legal tender, it means that cryptocurrency was largely unregulated, at the time the 2014 Position Paper was published and nor is it provided by any banking institutions. By applying this knowledge to the concept of e-money, it is

[22]E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[23] In determining a definition of what constitutes as 'e-money', SARB had referred to the National Payment System Department Position Paper on Electronic Money. South African Reserve Bank National Payment System Department op cit note 1 at 3.3; See also: A Niemand 'A Few South African Cents' Worth on Bitcoin' op cit note 16; E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[24] South African Reserve Bank National Payment System Department op cit note 1 at 3.3.

[25] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[26] Ibid.

determined that cryptocurrency does not fit within the scheme of what is considered to be e-money as it is unregulated.[27]

Furthermore, it was found that cryptocurrencies are also not considered to be a security.[28] According to the National Treasury:

> While virtual currencies [cryptocurrencies] can be bought and sold on various platforms, they are not defined as securities in terms of the Financial Markets Act, 2012 (Act No. 19 of 2012). The regulatory standards that apply to the trading of securities therefore do not apply to virtual currencies.[29]

Hence, through the 2014 Position Paper it can be noted that cryptocurrencies are understood as being a DCVC, and is not in any form a legal tender, nor security or e-money.

Through the 2019 Consultation Paper, the definitional understanding of cryptocurrency determined in the 2014 Position Paper was confirmed. Furthermore, through the 2019 Consultation Paper, it was confirmed that the term 'cryptocurrency' did not fit within the classification of legal tender.[30] The 2019 Consultation Paper also focussed on a functional approach and evolved the distinction of cryptocurrency into a more specific collective term known as a crypto asset.[31]

Regulatory bodies were of the opinion that the term 'cryptocurrency' would create confusion within the general public if it is associated with the term 'currency', when it is in fact not considered a legal tender.[32]

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[27] Ibid.

[28] It has been recommended by the 2020 Position Paper, to include initial coin offerings and security tokens within the term 'security', as found in the Financial Markets Act 19 of 2012. Further discussion on these forms of cryptocurrencies will be explored in chapter 2 as well as chapter 4.

[29] National Treasury, 'User alert: Monitoring of virtual currencies' National *Treasury* 2014, available at: *http://www.treasury.gov.za/comm_media/press/2014/2014091801<percent>20<percent>20User<percent>20Alert<percent>20Virtual<percent>20currencies.pdf,* accessed on 29 June 2020; See also: chapter 1 ss 30–55 of the Financial Market Act 19 of 2012; E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[30] Section 17 of the SARB Act provides that:

1. a tender is by the Bank itself, of a note of the Bank or of an outstanding note of another bank for which the Bank has assumed liability in terms of section 15 (3) (c) of the Currency and Banking Act or in terms of any agreement entered into with another bank before or after commencement of this Act; and
2. a tender by the Bank itself, of an undefaced and unmutilated coin which is lawfully in circulation in RSA and of current mass.

[31] In addition to being called a crypto asset, other terms such as digital tokens, digital assets, and crypto tokens are also used. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group *Consultation Paper on Policy Proposals for Crypto* (2019) at 2.1; See also: Committees on Payments and Market Infrastructures *Digital Currencies* 2015; E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[32] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6; See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 31.

Therefore, the term 'crypto asset' is utilised. The term, crypto asset, adequately encapsulates the nature of the DCVC not being a legal tender, but at the same time not losing the characteristics of being virtual, decentralised and convertible.[33]

Hence, the 2019 Consultation Paper defines a crypto asset as:

> …digital representations or tokens that are accessed, verified, transacted, and traded electronically by a community of users. Crypto assets are issued electronically by decentralised entities and have no legal tender status, and consequently are not considered as electronic money either. It therefore does not have statutory compensation arrangements. Crypto assets have the ability to be used for payments (exchange of such value) and for investment purposes by crypto asset users. Crypto assets have the ability to function as a medium of exchange, and/or unit of account and/or store of value within a community of crypto asset users.[34]

In deriving this term, the 2019 Consultation Paper took into account the various perspectives that had been established since 2014. Namely that many banking institutions do not regard crypto assets as a legal tender, nor was crypto assets considered to be a financial product. However, through its underlying nature, crypto assets are seen as a technology that facilitates a medium of exchange and is a representation of some form of value. Hence, the term crypto asset was adopted to encompass its said characteristics as well as the perspectives of various financial institutions.[35]

The 2020 Position Paper further confirmed the definition of a crypto asset, as found in the 2019 Consultation Paper.

However, in acknowledging that the term 'crypto asset' is a functional approach that encompasses both the economic nature and technological nature of crypto assets, the 2020 Position Paper further explained that crypto assets can be interpreted to relate to a collective term. By viewing crypto assets as a collective term, the 2020 Position Paper views this term to encompass the following:[36]

- Exchange or payment tokens such as cryptocurrencies like Bitcoin;[37]

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[33] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 31 at 2.1; See also: E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[34] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 6 at 2.1.2.

[35] The term crypto asset is also used by the European Central Bank. The European Central Bank confirms the term crypto asset, as it corresponds with a virtual currencies' characteristics. M T Chimienti, U Kochanska & A Pinna 'Understanding the crypto-asset phenomenon, its risks and measurement issues' (2019) 5 *European Central Bank Economic Bulletin*.

[36] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper on *Crypto Assets* (2020) at 2.1.3.

[37] Tokens that are used as a medium of exchange for payment of goods and services. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 36 at 2.1.3.

- Security tokens;[38]
- Utility tokens.[39]

Hence, through this 2020 Position Paper, the definition of a crypto asset that can be adopted by regulatory bodies is noted as being:

> A crypto asset is a digital representation of value that is not issued by a central bank, but is traded, transferred and stored electronically by natural and legal persons for the purpose of payment, investment and other forms of utility, and applies cryptography techniques in the underlying technology.[40]

However, as noted by the 2020 Position Paper, this definition does not include within its ambit the concept of Stablecoins. The term 'Stablecoins' refers to a type of crypto asset, that falls within the category of a cryptocurrency.[41] It has a reduced volatility in price when compared to traditional crypto assets.[42] The reason for this reduced-price volatility, is because Stablecoins have a form of a stability mechanism and collateral to ensure a reduction in its price volatility. In addition to this information, the stability mechanism related to the Stablecoin may be for example based on an algorithm or alternatively collateralised.[43] The type of collateral a Stablecoin may rely on, can include a fiat currency such as the Dollar or alternatively another crypto asset such as Bitcoin.[44]

In addition, the 2020 Position Paper acknowledges the fact that crypto assets are still not considered to be a form of legal tender. Furthermore, SARS provides a view to support the classification of cryptocurrency as an 'asset'. SARS views crypto assets as being an intangible asset, that is not in any form considered to be a legal tender.[45] In coming to this view, SARS determined that within the Income Tax Act,[46] there is no definition of a 'currency'. However, SARS is of the understanding that cryptocurrencies do not also fall within the ambit of the meaning of 'legal tender'. In addition to these understandings, SARS also highlights the fact they do not view cryptocurrencies as being a medium of

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[38] Tokens that provide ownership rights, entitlements or a share in profits. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 36 at 2.1.3.
[39] Tokens that can be redeemed for goods and services found within the blockchain. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 36 at 2.1.3.
[40] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 36 at 2.1.4.
[41] A Berentsen & F Shar *Stablecoins: The quest for a low- volatility cryptocurrency* (2019) at 65-71; See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 36 at 2.1.4.
[42] Ibid.
[43] Ibid.
[44] Ibid.
[45] 'Sars stance on the tax treatment of cryptocurrencies' SARS 6 April 2018, available at: *https://www.sars.gov.za/Media/MediaReleases/Pages/6-April-2018---SARS-stance-on-the-tax-treatment-of-cryptocurrencies-.aspx* , accessed on 24 May 2020.
[46] Income Tax Act 58 of 1962.

exchange as it is not widely used or accepted. Hence, through these views, SARS does not view a cryptocurrency as a currency or legal tender, but instead as an intangible asset.[47]

Therefore, it can be seen that the definition of a cryptocurrency has been continuously developed through the years since the 2014 Position Paper to give greater clarity. Furthermore, 'cryptocurrency' can therefore best be understood to be a subset of a crypto asset.[48]

This continuous analysis and development of the concept of cryptocurrency serves as evidence to show that regulatory bodies aim to ensure there is a holistic understanding of the definition of this financial technology. Although the definition as understood in the 2020 Position paper does not include Stablecoins within its ambit, it can be inferred that through further analysis of the definition, the concept of a Stablecoin may, in the future be included within the term of 'crypto asset' as understood by the IFWG CARWG.

The definition of a cryptocurrency is pivotal to this research paper. This definition influences the way that existing legislation would need to be interpreted and applied, in order for there to be cryptocurrency regulation.

It can, therefore, be observed that in terms of the 2014 Position Paper, a technical classification of Virtual Currency was adopted, with cryptocurrency falling within the ambit of a Virtual Currency in terms of a DCVC. However, through the 2019 Consultation Paper, and 2020 Position Paper, the understanding and definition of cryptocurrency was further developed. It was determined that a cryptocurrency can further be categorised as being a subset that falls under the general classification known as a crypto asset. Hence, an evolution of the understanding of a cryptocurrency can be observed.

Consequently, it can be noted that this dissertation, like the 2020 Position Paper will utilise the terms crypto asset and, cryptocurrency where applicable, as crypto assets are seen as a collective term that encompasses the subset known as cryptocurrency.

b) Characteristics

Crypto assets are characterised as being a DCVC (as explained above) and cannot be considered a legal tender.[49]

[47] 'Sars stance on the tax treatment of cryptocurrencies' op cit note 45.
[48] 'A look at current financial reporting issues' *PWC* 2019, available at: *https://www.pwc.com/gx/en/audit-services/ifrs/publications/ifrs-16/cryptographic-assets-related-transactions-accounting-considerations-ifrs-pwc-in-depth.pdf,* accessed on 14 February 2020.
[49] Refer to chapter 2, Section II.

Furthermore, from a more technical stand point, the foundation of crypto assets can be seen as being based on block chain and cryptography technology that is mathematics based, with peer-to-peer and open-source networking.[50]

In addition to the characteristics mentioned above, crypto assets are also pseudonymous.[51] This means that the actual details, or context of the transaction are public, but the identities of the parties to the transaction will be anonymous. In addition to this, crypto asset transactions are instantaneous, irreversible and lastly secure through encryption.[52]

In terms of a crypto asset's security, it is based on a concept known as cryptography. Cryptography in its most basic form refers to the protection or communication of information through the use of codes, allowing only those for whom the information is intended, to process the codes in order to have access to the information. By looking at cryptography in the context of crypto assets, it refers to protecting the transaction, the ability to remain decentralised, and preventing double spending[53] of cryptocurrencies.[54]

It is through cryptography that the characteristic of a crypto asset (being pseudonymous) is achieved. Through cryptography, an encrypted[55] message is sent by the sender of the crypto asset. Encryption occurs through the use of an algorithm. Once the message is received, the recipient will decrypt the encrypted message, thereby receiving the crypto asset. Hence, through cryptography, it ensures that transactions are secure for all parties involved.[56]

III. TECHNOLOGY

Crypto assets are forms of Fintech, and the technology that underpins crypto assets are based on blockchain technology. This technology is secured through cryptography and encryption. The

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[50] South African Reserve Bank National Payment System Department op cit note 1 at 2. Both block chain and cryptography technology will be further explained later on in this chapter.

[51] A Rosic 'What is Cryptocurrency? [Everything You Need to Know!]' *Blockgeeks* 2016, available on: *https://blockgeeks.com/guides/what-is-cryptocurrency/ ,* accessed on: 23 May 2020.

[52] Ibid; See also: In addition to advantages using crypto assets, it can be noted that there are various disadvantages associated with crypto assets. Such disadvantages may include the volatility associated with crypto assets as well as the risk associated with investing in cryptocurrencies. Other disadvantages associated with crypto assets use may include money laundering the financing of terrorist activity. F Bunjaku, O Gjorgieva-Trajkovska & E Miteva-Kacarski 'Cryptocurrencies – Advantages and Disadvantages' (2017) 2 *Journal of Economics* at 31-39.

[53] Double spending is a concept that refers to crypto asset transactions that are duplicated and are spent twice due to digital information being copied or reproduced. Double spending is prevented through cryptography, namely in combination with blockchain technology and encryption. J Frankenfield 'Double-Spending' *Investopedia* 30 June 2020, available on: *https://www.investopedia.com/terms/d/doublespending.asp*, accessed on: 1 July 2020.

[54] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6; See Also: K Richards 'Cryptography' *Tech Target* 2020, available on: *https://searchsecurity.techtarget.com/definition/cryptography*, accessed on 27 September 2021.

[55] Encryption will be further discussed within Section III of this chapter.

[56] S Seth 'Explaining the Crypto in Cryptocurrency' *Investopedia* 25 January 2020, available on: *https://www.investopedia.com/tech/explaining-crypto-cryptocurrency/ ,* accessed on 23 May 2020.

framework of crypto assets is founded on the premise of an open based, peer-to-peer system. This framework is supported through protocols that are created through crypto-miners.[57]

a) Blockchain

Blockchain is a technology that is the foundation of crypto assets. Upon being invented by Satoshi Nakamoto, the primary use for blockchain was determined to be used for digital currencies. Blockchain is essentially a public ledger that contains all crypto asset transactions that have ever occurred.[58]

Blockchains are commonly referred to as a distributed ledger or alternatively a public ledger. Simply put, this technology is seen as being a permanent record of transactions or data.[59] For a blockchain to exist, a transaction has to be confirmed.[60] Once a transaction is confirmed, according to the author Ameer Rosic, a crypto asset transaction becomes '…no longer forgeable, it can't be reversed, it is part of an immutable record of historical transactions: of the so-called blockchain.'[61] Hence this prevents a transaction from being forged or duplicated.

Although blockchain is primarily associated with crypto assets, this technology has through the years advanced gradually, not only to be applied to crypto assets, but also to be applicable towards non-crypto applications. Hence, examples of non-crypto applications may include smart contracts, smart property and even music royalties.[62]

b) Mining

Crypto-mining may be done by any individual who has access to computer equipment that is built specifically for the purpose to mine crypto assets. Although crypto assets are decentralised, this does not mean that transactions are not verified. For crypto assets, transactions are verified through crypto-

[57] For a detailed explanation on crypto asset mining, refer to Sub-Section b of Section II, within chapter 2. S Hughs, S Middlebrook 'Advancing a Framework for Regulating Cryptocurrency Payments Intermediaries' op cit note 5.
[58] A Rosic 'What is Blockchain Technology? A Step-by-Step Guide for Beginners' *Blockgeeks* 2015, available on: *https://blockgeeks.com/guides/what-is-blockchain-technology/*, accessed on: 23 May 2020.
[59] B Geva & J Cheng 'Understanding Block Chain and Distributed Financial Technology: New Rails For Payments and an Analysis of Article 4a of the UCC' (2016) 25 *Business Law Today* at 1-5.
[60] Ibid.
[61] A Rosic 'What is Cryptocurrency? [Everything You Need to Know!]'op cit note 51.
[62] The most common application can come in the form of a smart contract. Through a blockchain the smart contract can be programmed to self-execute and self-maintain, once all terms of the contract have been met. For a smart contract, normally an intermediary ensures all parties follow through on the terms of a conventional contract. However, blockchains waves the need for third parties and ensures that all blockchain participants know the contract details and that contractual terms are implemented automatically once conditions are met. Blockchain can also be applied to musicians. Music, especially digital music face major issues regarding piracy, ownership as well as royalties paid to musicians. Through the use of blockchain and smart contracts, a database of music rights can be created and furthermore through blockchain it will allow for a transparent transaction of royalties as well as real-time distribution of music by relying on the technology. There are many other applications of blockchain, such as to smart property, healthcare and appliances. A Rosic, '17 Blockchain Applications That Are Transforming Society', Block Geeks 2017, available at: https://blockgeeks.com/guides/blockchain-applications/#comments, accessed on: 25 February 2020; See also: M Crosby, Nachiappan, P Pattanayak, S Verma & V Kalyanaraman 'Blockchain Technology: Beyond Bitcoin' (2016) 2 Applied Innovation Review.

mining. Once a transaction is verified through crypto-mining, the transaction — which is a 'block' — is then added to a chain of other verified transactions, hence forming a blockchain.[63]

Mining refers to solving mathematical puzzles. The miner who solves the puzzle first, will place the block on the chain and the transaction will be verified. A reward of crypto assets is offered to miners who solve these puzzles.[64]

There are different forms of consensus mechanisms that are utilised by miners to verify crypto asset transactions. These methods include Proof-of-Work (PoW) and Proof-of-Stake (PoS). In terms of a PoW, miners solve mathematical equations that would validate the transactions, therefore when the solution is solved, a new block is added to the blockchain. Miners are then rewarded a Bitcoin for their validation. Miners mining Bitcoin rely on this consensus method.[65] In terms of PoS, the miner that mines the most coins would validate the transaction. Miners mining Peercoin, Dash, and Nexus rely on this method.[66] These particular methods are dependent on the particular type crypto asset that is being mined.[67]

There are also to various ways that are relied upon by miners to institute the relevant consensus mechanism. These include, cloud mining and hardware mining.[68]

Hence, it can be noted that mining can be seen as the equivalent to mining of minerals in the real world, whereby there is a financial gain for 'mining'. Consequently, just as how mining in the real world is costly, so is mining of crypto assets as it requires sophisticated hardware and a large amount of energy.

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[63] Intergovernmental Fintech Working Group, Crypto Assets Regulatory Working Group Position Paper op cit note 36 at 3.6.3.

[64] Ibid.

[65] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[66] Ibid.

[67] Ibid.

[68] Cloud mining refers to renting hardware and having someone else mine for an individual. A contract will occur between the cloud mining company and the individual requesting their services. Once the contract is agreed upon, the individual may be required to choose a mining pool, which is where miners collaborate with one another in order to increase their chances of mining cryptocurrencies. Hardware mining refers to obtaining a computer, through specialised hardware. Each particular component of the specialised hardware provides a form of computational power required for crypto asset mining. The greater the computational power of a computer, the more successful a miner will be in finding cryptocurrencies. Specialised Hardware includes:

- central processing units (CPUs);
- graphic processing units (GPUs);
- field programmable gate arrays (FPGAs); and
- application specific integrated circuits (ASICs).

Each particular component provides a form of computational power required for crypto asset mining. J Martindale 'How to mine Bitcoin' *Digital Trends* 2020, available at: *https://www.digitaltrends.com/computing/how-to-mine-bitcoin/*, accessed on: 4 June 2020.

c) Peer-to-Peer Network (P2P Network)

Crypto assets operate within a P2P Network. This particular network operates when there are two or more devices or nodes[69] connected to the internet. These devices then communicate data between each other. By having multiple devices communicating with one another, it creates a network system where there is not a single central server, but instead a decentralised server with multiple computers communicating with each other.[70]

The users or participants in this particular network are called peers and are identical to one another.[71]

Furthermore, it must also be noted that open-source software (OSS) compliments a P2P Network. OSS allows a network to be decentralised and operate without the need of a central server. An example of an OSS is Bitcoin Core, which is an OSS utilised for facilitating Bitcoin transactions.[72]

d) Encryption

As indicated within the characteristics of crypto assets, cryptography provides a form of security for cryptocurrency transactions. Cryptography[73] secures cryptocurrency through encryption.

Encryption refers to when information is rendered to be unreadable, hence making it accessible only to a person who has a decryption key or password to decrypt the respective information.[74]

Encryption ensures that the information is safely delivered to the recipient and that the information is only accessible by the sender of the information and the recipient of the information, both who have a decryption key.[75] There are three forms of encryption, and they are:[76]

- Symmetric encryption;
- Asymmetric encryption; and

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[69] A node refers to a computer that is connected to a P2P network. Nodes support the P2P network through validation transactions and transmitting transactions, which result in a copy of the block chain that is accessible to the node. 'Node (cryptocurrency network) – definition and examples' *Market Business News*, available on: *https://marketbusinessnews.com/financial-glossary/node-cryptocurrency-network/,* accessed on 2 June 2020.

[70] 'What is a peer-to-peer network?' *Luno* 2016, available on: *https://www.luno.com/learn/en/article/what-is-a-peer-to-peer-network*, accessed on 28 May 2020.

[71] A Rosic 'What is Blockchain Technology? A Step-by-Step Guide For Beginners' op cit note 60.

[72] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

[73] The Electronic Communications and Transactions Act (ECT Act) refers to 'cryptography' products within section one of the act. Through the act's definition of cryptography, it can be deduced that crypto assets, and its respective transactions fall within the ECT Act definition of cryptography. Chapter 5 of the ECT Act furthermore makes provision for cryptography. Within this chapter it ensures that cryptography service providers provide a register of the names and addresses of their clients as well as a register of their products and a description of the products offered (in relation to cryptography) to the Department of Communication, failure of which would result in the service provider not being able to operate legally. 'Cryptography laws in South Africa' *Michaelsons* 2019, available on: *https://www.michalsons.com/blog/cryptography-laws-in-south-africa/3266,* accessed on 29 June 2020.

[74] N Lord 'What Is Data Encryption? Definition, Best Practices & More' *Digital Guardian* 2019, available on: *https://digitalguardian.com/blog/what-data-encryption*, accessed in: 23 May 2020.

[75] Ibid.

[76] S Seth 'Explaining the Crypto in Cryptocurrency' op cit note 56.

- Hashing.

In terms of symmetric encryption, this form of encryption relies solely on a single matching key that respectively encrypts and decrypts any messages sent and received. The sender will need to exchange the key with the receiver.[77]

Asymmetric encryption on the other hand, makes use of two keys, namely a public key and a private key. The public key is used by the sender to encrypt data and this key is sent openly to the public. The recipient however, is in possession of a private key, which is only known to the recipient. The private key is used to decrypt any data that is received.[78] This particular encryption method is used for Bitcoin transactions.[79] Furthermore, the private and public keys are encrypted in the form of SHA-256.[80]

In addition, crypto assets rely on a concept known as hashing. Hashing ensures the integrity of data within the P2P network.[81]

A crypto asset transaction is therefore initiated when an individual makes a request for a transaction (the sender). This transaction request is then sent to a P2P network, which is decentralised and operates through nodes. The nodes are connected to the P2P network. Therefore, through this network, crypto-miners will validate the requested transaction through solving complex mathematical equations. Once a crypto-miner has solved the equation, the requested transaction is then validated, and will form a new block of information. This new block will then be added to an existing growing chain of blocks, hence forming a block chain. The transaction will then be complete and would be ready to be received by the recipient of the crypto asset. Throughout this entire transaction process, the transaction is encrypted.[82]

IV. TYPES OF CRYPTO ASSETS

It is important to understand that various forms of crypto assets exist currently, and it is also necessary to identify these variations in order to conceptualise as well as implement regulations that would apply to crypto assets.[83]

There are various types of crypto assets, each having their own justification for their existence, and these can include cryptocurrencies, tokens and initial coin offerings (ICO).[84]

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[77] Ibid.
[78] Böhme et al (2015) 29(2) *The Journal of Economic Perspectives* 213 at 216. For a discussion of the different types of cryptography application, See also: E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies 'op cit note 6.
[79] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.
[80] Commonly known as Secure Hash Algorithm 256bit. Ibid.
[81] S Seth 'Explaining the Crypto in Cryptocurrency' op cit note 56.
[82] Ibid.
[83] Jabotinsky & Hadar 'The Regulation of Cryptocurrencies-Between a Currency and a Financial Product' 2018 *SSRN Electronic Journal*.
[84] Ibid.

Crypto assets, and namely its subset cryptocurrency can be categorised as:[85]

- First generation;
- Second generation; and
- Third generation

a) First Generation

In 2008, Satoshi Nakamoto created the concept of blockchain,[86] which serves as a distributed ledger with its relevant protocols for cryptocurrency, namely the first cryptocurrency, which is known as Bitcoin.[87]

Bitcoin was envisioned to be an electronic payment system that is supported and based on blockchain technology. Through Bitcoin, two parties would be able to initiate transactions that are pseudonymous, instant, publicly available and without the need of facilitation by a third party like a bank. Hence a transaction would occur solely between two willing parties who have the intention to transact between each other. Furthermore, through blockchain technology, transactions were protected against fraud, hence protecting parties to a transaction. It was intended by Satoshi Nakamoto to create a decentralised medium of exchange.[88]

Upon the introduction of Bitcoin, the cryptocurrency was subsequently modified to form variations of Bitcoin. These variations formed part of the first-generation crypto assets, but were known as Alt-coins instead. These Alt-coins differed to Bitcoin, namely because they were created through a variation of the Bitcoin source code. In essence, all other forms of cryptocurrencies other than Bitcoin, are seen as Alt-coins. Furthermore, the relevant Alt-coin had its logo changed so that it does not identify with Bitcoin, and lastly its cryptographic hash was changed. Examples of Alt-coins include Litecoin.[89]

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[85] K Spurjeon, S Sahu & A Dutta 'Survey on cryptocurrency technology '(2018) 8 *International Journal of Advanced Management, Technology and Engineering Sciences.*

[86] Detailed description of blockchain is discussed within Section III of chapter 2.

[87] 'A Survey on Blockchain Technology and its Proposed Solutions' *Science Direct* 2019, available on: *https://www.sciencedirect.com/science/article/pii/S187705091931717X*, accessed on: 24 May 2020.

[88] S Nakamato 'Bitcoin: A Peer-to-Peer Electronic Cash System '2008, available at https://www.bitcoin.org/bitcoin pdf, accessed on 27 May 2020.

[89] Through Alt-coin's varied source code, it was able to make improvements to the perceived shortcomings of Bitcoin. These improvements included in the time to mine the relevant coins. A Bitcoin required ten minutes to mine, whilst an Alt-coin like Litecoin only required two and a half minutes to mine. Furthermore, Alt-coins provide more variety and competition than having a single Bitcoin. In addition, Bitcoin require complex computer equipment for mining, and in comparison, Alt-coins like Litecoin require relatively simple and ordinary computer equipment to mine. However, Alt-coins when compared to Bitcoin, are relatively unstable, with their value being unpredictable due to its novelty and volatility. 'ELI5 First, second and third generation cryptocurrencies' *Crypto* 2018, available on: *https://crypto.bi/tape/generations/*, accessed on: 29 May 2020; See also: D Bradberry 'What are Alt-coins?' *The Balance* 2020, available on: *https://www.thebalance.com/altcoins-a-basic-guide-391206*, accessed on: 29 June 2020.

b) Second Generation

This generation introduced a new facet to cryptocurrency, in the form of Ethereum.[90] Unlike Alt-coins, Ethereum was not merely a variation of a Bitcoin,[91] but instead was a completely new form of cryptocurrency that is derived from the Turing complete language.[92] Ethereum is not simply a form of medium of exchange like Bitcoin, but is more distinct and smarter than Bitcoin.[93]

Through its unique format, Ethereum is able to facilitate smart contracts,[94] smart property[95] and distributed applications.[96] Ethereum can also be used to create new crypto assets easily and efficiently, such as its own native cryptocurrency known as Ether. The characteristics of Ether are identical to that of Bitcoin — a decentralised, anonymous, medium of exchange.[97]

c) Third Generation

Third generation cryptocurrency built further on the concept of the second generation. However, third generation cryptocurrency is not commonly used when compared to both first and second-generation cryptocurrency. The main objective of third generation cryptocurrencies is the need for a governance

[90] The Ethereum white paper was originally published in 2013 by V Buterin, the founder of Ethereum, before the project's launch in 2015; See also: 'Ethereum Whitepaper' *Ethereum* 2020, available on: *https://ethereum.org/whitepaper/*, accessed on: 29 May 2020.

[91] Bitcoin relied on the C++ language. This particular language is defined as a general-purpose programming language that forms the source code of Bitcoin. 'Learn C++ Programming' *Programiz*, available on: *https://www.programiz.com/cpp-programming*, accessed on: 29 June 2020; See also: J Harm, J Obregon, J Stubbendick 'Ethereum v Bitcoin' *Economist*, available at: *https://www.economist.com/sites/default/files/creighton_university_kraken_case_study.pdf,* accessed on: 29 June 2020.

[92] Turing Complete Language refers to most regular programming languages such as JavaScript, Lua, C++, C#, C and Python. Turning languages allows Ethereum to 'solve problems. Ethereum is seen as being Turing language complete as it has the ability and purpose to solve problems, i.e., Ethereum, through Turning Languages has the ability to understand terms and conditions of agreements that form smart contracts. Contrasting Ethereum, Bitcoin is seen as being Turing incomplete, as its only purpose in terms of its C++ programming is to serve as a payment system. Other programming languages do not form Bitcoin; hence it is Turing incomplete and cannot solve problems like Ethereum. 'Turing Complete' *Binance Academy*, available at: *https://academy.binance.com/glossary/turing-complete*, accessed on: 29 June 2020.

[93] J Harm, J Obregon, J Stubbendick 'Ethereum v Bitcoin' op cit note 91.

[94] Smart contracts are essentially a protocol found within the Ethereum block chain. It is a binding contract that consists of a set of terms and conditions. A smart contract shares the same characteristics as a traditional contract, which is to execute the terms and conditions of a contract. However, a smart contract is self-executing and has a storage-based variable, due to the fact it is based on block chain. It is also governed by common law, just like regular contracts. S Govender 'Smart Contracts vs Traditional Contracts: Same but Different 'Webber Wentzel 13 March 2019, available at https//www.webberwentzel.com/News/Pages/smart-contracts-vs-traditional-contracts-same-but- different.aspx, accessed on 29 May 2020.

[95] Much like a smart contract, ownership of property can be implemented through a protocol within Ethereum. V Buterin 'Ethereum White Paper: A next Generation Smart Contract and Decentralised Application Platform' op cit note 90; See also: S Govender 'Smart Contracts vs Traditional Contracts: Same but Different' op cit note 94.

[96] Ethereum is required to create decentralised applications. Decentralised applications are characterised by being open source, decentralised, incentivised and lastly, it uses a particular protocol, in Ethereum's case—PoW. Distributed applications may be used to plan resources for a company or alternatively be involved in asset management. 'What Are Dapps? The New Decentralized Future' *Blockgeeks* 2019, available at: *https://blockgeeks.com/guides/dapps/*, accessed on: 29 June 2020.

[97] 'ELI5 First, second and third generation cryptocurrencies' op cit note 89.

system, reduced scalability, and interoperability. Cardano is an example of a third-generation cryptocurrency. [98]

d) Tokens

Crypto assets also encompass crypto tokens or just simply, tokens.[99] Tokens may be perceived as being having a specific use or protocol on a block chain.[100]

According to the IFWG 2020 Position Paper tokens may include:[101]

A. Exchange or payment token;[102]
B. Security token;[103] and
C. Utility token.[104]

e) Initial Coin Offerings

Initial coin offerings (ICO) are used to increase funds or capital of a business or company using blockchain technology. Essentially, if a company requires funding, an ICO will be issued, where the issuer will collect the investment that will be used to finance the particular project. The investment made would be in the form of the investor purchasing tokens, hence the investor, in return for making an investment will receive a token. This particular token is a crypto asset that may be an exchange or payment token, security token or even a utility token.[105] In essence, an ICO is a crypto asset's version of an Initial Public Offering.[106]

[98] K Spurjeon, S Sahu, A Dutta 'Survey on cryptocurrency technology 'op cit note 87; See also: 'ELI5 First, second and third generation cryptocurrencies' op cit note 89.
[99] E Reddy, V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies 'op cit note 6.
[100] K Kopke 'How do you classify cryptocurrency as an investment?' (2018) 18 *Without Prejudice* 2; See also: K Mitchell 'Blockchain IPOs: Capital Raising in the Crypto-World' (2019) 19 *Without Prejudice* 1; J Frankenfield 'Crypto Tokens' *Investopedia* 2018, available at: *https://www.investopedia.com/terms/c/crypto-token.asp*, accessed on: 2 June 2020.
[101] Intergovernmental Fintech Working Group Crypto Assets Working Group Position Paper op cit note 36 at 2.1.3.
[102] Tokens that are used as a medium of exchange for payment of goods and services. Intergovernmental Fintech Working Group Crypto Assets Working Group Position Paper op cit note 36 at 2.1.3.
[103] Tokens that provide ownership rights, entitlements or a share in profits. Intergovernmental Fintech Working Group Crypto Assets Working Group Position Paper op cit note 36 at 2.1.3.
[104] Tokens that can be redeemed for goods or services found within the blockchain. Intergovernmental Fintech Working Group Crypto Assets Working Group Position Paper op cit note 36 at 2.1.3.
[105] Intergovernmental Fintech Working Group Crypto Assets Working Group Position Paper op cit note 36 at 3.4.
[106] An initial public offering (IPO) refers to the process of offering shares of a private corporation to the public in a new stock issuance. Public share issuance allows a company to raise capital from public investors. A Hayes 'Initial Public Offering' *Investopedia* 2020, available at: *https://www.investopedia.com/terms/i/ipo.asp*, accessed on 1 June 2020; See also: K Kopke 'How do you classify cryptocurrency as an investment?' op cit note 100; K Mitchell 'Blockchain IPOs: Capital Raising in the Crypto-World' op cit note 100; J Frankenfield 'Crypto Tokens' op cit note 100.

V. OBTAINING CRYPTO ASSETS

In recognising the foundations as well as technology behind crypto assets, it is also important to understand the manner in which cryptocurrencies, as well as crypto assets may be obtained. There are various methods available to obtain crypto assets. These methods include:

A. Exchanges;

B. Merchants;[107]

C. Cryptocurrency Automated Teller Machine (CATM); and

D. Miners.[108]

In addition to these methods, it is important to note that an Open-Source Software (OSS) is required, in order to facilitate any form of cryptocurrency. In the case of Bitcoin, an OSS known as Bitcoin Core is required to facilitate this crypto asset.[109]

a) Exchanges

Exchanges are seen as a digital store where an individual can purchase or sell crypto assets in return for its equivalent value in fiat currency.[110] Within South Africa therefore, crypto assets may be purchased using credit cards, debit cards and electronic fund transfers.[111] Within South Africa, the most common exchange platforms are Luno,[112] Altcoin Trader,[113] and VALR.[114]

It must be noted that although crypto assets are decentralised, through the use of exchanges, it allows regulators to impose an indirect form of regulation over crypto assets that allows the identities of those that trade crypto assets to be known. Exchange platforms such as Luno require Know-Your-Customer (KYC) protocols to ensure that they are FICA compliant. Hence, through these exchanges, it is possible to have a record and identify clients who may flout certain regulations.[115] Hence, by exchanges instituting KYC protocols and due diligence procedures, it can enable financial regulators to monitor and prevent the illicit use of crypto assets.

However, although there are KYC and FICA protocols in place within South Africa, there are also many exchanges that operate legally in foreign jurisdictions that either have partial or completely

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[107] This refers to the purchasing of goods or services through crypto assets.
[108] Discussed above, in chapter 2, Section III, Sub-Section b of this Dissertation.
[109] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.
[110] A Nieman 'A few South African cent's worth on Bitcoin 'op cit note 16.
[111] Ibid.
[112] Luno is available to be accessed at: *https://www.luno.com/en/*.
[113] Altcoin Trader is available to be accessed at: https://www.altcointrader.co.za.
[114] VALR is available to be accessed at: https://www.valr.com; See also: L Schoeman 'How to buy Bitcoin in South Africa (Legally)' *SA Shares* 2020, available at: *https://www.sashares.co.za/how-to-buy-bitcoin-in-south-africa/#gs.876dv8*, accessed on 2 June 2020.
[115] E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies' op cit note 6.

no requirement for KYC, when crypto asset transactions are entered into. Hence, such exchanges may prove difficult to regulate within the South African landscape, as it can allow users of these exchanges to flout South African regulations such as KYC protocols and FICA.[116]

b) Merchants

A merchant refers to a store or individual that offers goods and services for a price that is sold for profit to a customer. There are various types of merchants such as those that deal within e-commerce, retailers as well as wholesalers.[117]

All of these types of merchants, may accept electronic fund transactions, cash or even credit payments for goods and services. However, through the introduction of crypto assets many merchants have started to accept cryptocurrencies such as Bitcoin and Ethereum in exchange for goods and services.[118]

Within South Africa, the popularity of Bitcoin has been recognised with prominent online merchant Takealot allowing payments to be processed via Bitcoin.[119]

c) CATM

CATM refers to a form of automated teller machine that exclusively deals with cryptocurrencies. CATM's allow individuals to purchase or even sell Bitcoins and other cryptocurrencies. A CATM is connected to the internet and allows users to request transactions such as deposits[120] or withdrawals.[121]

A major difference between traditional bank ATM's and CATM's is that CATM's are not owned or managed by any financial institutions like traditional bank ATM's.[122]

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[116] Examples of exchanges that require partial or no KYC protocols include: Nominex, Bybit, Binance, Bitmax and Kucoin. For further reading please refer to: *https://news.bitcoin.com/6-cryptocurrency-exchanges-that-dont-require-kyc/.*

[117] 'What is a merchant' *E Commerce Platforms*, available at: *https://ecommerce-platforms.com/glossary/merchant*, accessed on: 2 June 2020.

[118] Ibid.

[119] A Nieman 'A few South African cent's worth on Bitcoin' op cit note 16; See also: Furthermore, retail shops such as Jekyll & Hyde, sell leather goods via Bitcoin, in addition to traditional forms of payment. Online clothing retailers, Superballist are also now accepting payments in the form of crypto assets like Bitcoin. Local supermarkets such as Pick n Pay are also offering consumers the chance to pay with Bitcoin through their in-store trial of the transaction process. The trial process was conducted to determine its effectiveness as an alternate means of payment, however implementation of this form of payment would only be standardised to other Pick n Pay stores once there is clearer guidance as well as more precise regulatory framework governing Bitcoin and crypto assets. '5 Retailers in SA That Accept Bitcoins' *Menstuff* 2018, available at: *https://www.menstuff.co.za/lifestyle/5-retailers-in-sa-that-accept-bitcoin/*, accessed on 2 June 2020; See also: D Mcleod 'Pick n Pay in in-store trial of bitcoin payments' *Tech Central* 2017, available at: *https://techcentral.co.za/bitcoin-now-accepted-pick-n-pay/77019/*, accessed on 3 June 2020.

[120] Individuals may transfer cash to purchase crypto assets which would be deposited into their e-wallets.

[121] Individuals would sell their crypto assets from their e-wallets and receive cash for it in return. J Frankenfield, 'Bitcoin ATM' *Investopedia* 2018, available at: *https://www.investopedia.com/terms/b/bitcoin-atm.asp*, accessed on: 3 June 2020.

[122] Through CATM's, customers may buy a whole or a partial number of Bitcoins. When a deposit or withdrawal is made, the CATM customer will be charged a service fee in the form of a percentage of the respective transaction. Within South Africa, the first CATM was launched in 2018 at a Spar supermarket in Johannesburg. However, this particular CATM is only able to facilitate deposits of crypto assets, such as Bitcoin, Ethereum and Litecoin, through cash purchases. T Rangongo 'Watch: SA's first ATM for Bitcoin and other cryptocurrencies in action' *Business Insider South Africa* 2018,

VI. STORAGE OF CRYPTO ASSETS

Once an individual has obtained a cryptocurrency like Bitcoin, the cryptocurrency will need to be stored within a 'digital wallet'. These wallets provide for the storage of cryptocurrency once they are acquired.[123]

The concept of a wallet does not merely refer to the literal meaning of a wallet, namely a place where money is stored, but in the case of crypto assets, a wallet refers to the storing of private keys that make up a particular address of a crypto asset.[124] A respective crypto asset transaction would result in two keys being produced, namely a private and public key.[125]

The public key is of public knowledge and used for identification of the crypto asset, whilst private keys are not of public knowledge and is only known by the wallet holder for the purposes of authentication, encryption and ownership of the respective crypto asset.[126] There are 4 different types of wallets that may be utilised by an individual. These wallets include the following:[127]

A. Software Wallet;[128]
B. Hardware Wallet;[129]
C. Paper Wallet;[130] and
D. Web Wallet.[131]

available at*: https://www.businessinsider.co.za/sas-first-cryptocurrency-atm-officially- launches-today-here-is-how-it-works-2018-5*, accessed on: 4 June 2020; See also: J Frankenfield, 'Bitcoin ATM' op cit note 121.

[123] Ibid.

[124] J Tuwiner 'What is a Bitcoin wallet?' Buy Bitcoin Worldwide 2020, available at: *https://www.buybitcoinworldwide.com/wallets/what-is/*, accessed on: 5 June 2020; See also: N Kaplanov, 'Nerdy Money: Bitcoin, the Private Digital Currency, and the Case Against its Regulation' (2012) 25 *Loyola Consumer Law Review* at 123.

[125] N Plassarass 'Regulating digital currencies: Bringing Bitcoin within the reach of the IMF '(2013) 14 *Chicago Journal of International Law*.

[126] 'Public and Private Keys' *Blockchain* 2020, available at: *https://support.blockchain.com/hc/en-us/articles/360000951966-Public-and-private-keys*, accessed on: 4 June 2020.

[127] J Tuwiner 'What is a Bitcoin wallet?' op cit note 124; See also: It is important to note that cryptocurrency wallets may be considered as being a 'hot wallet' or 'cold wallet'. A hot wallet refers to a wallet that is connected to the internet, whilst a cold wallet is a wallet that is not connected to the internet in any way; See also: A G. Khan, A H. Zahid, M Hussain and U. Riaz 'Security Of Cryptocurrency Using Hardware Wallet And QR Code' *2019 International Conference on Innovative Computing* 2019 at 1-10.

[128] This refers to a wallet where an individual would download an application on their computer device to store crypto assets. J Tuwiner 'What is a Bitcoin wallet?' op cit note 124.

[129] This refers to a device designed with the primary function to only store crypto assets. It keeps private keys away from internet connected devices and allows transactions to occur when offline. J Tuwiner 'What is a Bitcoin wallet?' op cit note 124.

[130] This refers to private keys being written or printed on paper rather than stored on a computer. J Tuwiner 'What is a Bitcoin wallet?' op cit note 124.

[131] This is a wallet where private keys are stored on a cloud service, allowing users to have access to their crypto assets from multiple devices. J Tuwiner 'What is a Bitcoin wallet?' op cit note 124.

VII. CONCLUSION

By analysing the legal concepts of crypto assets, as well as the classifications and definitions proposed by SARB, it illustrates that crypto assets are distinct to existing legal tender. The existing definition of a crypto asset is based on mere interpretation and comparison of the characteristics of crypto assets against other financial terms. Although crypto assets do share certain similarities with other defined financial terms, it must still be considered as being unique and independent. It can therefore be said, by understanding the concept of what constitutes as a crypto asset, and the unique nature of this technology—it would provide greater insight in understanding the concept of a crypto asset, which will allow regulators to determine whether legislation requires further amendment or development, to be in line with a crypto asset's definition.

CHAPTER 3

AN ANALYSIS OF SOUTH AFRICAN CRYPTO ASSET POSITION PAPERS

I. CHAPTER OVERVIEW

The purpose of this chapter is to analyse the three position papers that have been released by regulatory bodies in South Africa to date. These position papers provide an overview in terms of the stance applied by the regulatory bodies in relation to understanding and developing regulatory measures for cryptocurrencies.

The 2014 Position Paper was published by SARB and provided a foundational understanding towards the novel concept of cryptocurrencies. Furthermore, this particular position paper emphasised the risks associated with dealing with cryptocurrencies. It must be noted that at the time this paper was published, a clear definition as well as understanding on the concept of cryptocurrencies within South Africa was undeveloped. Through this paper, a definitional foundation was established, providing the platform for future papers to build on and further develop a holistic definition that could be applied by regulatory bodies. Furthermore, the 2014 Position Paper established certain risks that may be present when dealing with crypto assets. In identifying these risks, no solutions were proposed at that point in time by SARB to remedy what it perceived to be the risks.[1]

The initial 2014 Position Paper was followed by the 2019 Consultation Paper, which was published by the IFWG and CARWG. This paper had the aim of providing policy proposals for the regulation of crypto assets. The 2019 Consultation Paper further evolved the definition of a cryptocurrency and introduced the term 'crypto asset'.[2] The term crypto asset as opposed to cryptocurrency is continually utilised in the 2019 Consultation Paper and highlights the changed thinking in relation to the understanding of crypto assets and cryptocurrencies.

This paper built on the findings contained within the 2014 Position Paper and acknowledged these findings. In addition to these findings, the 2019 Consultation Paper acknowledged that since 2014, the following was considered:[3]

- The material impact crypto assets have on the financial services, such as payments, investments and capital raising.

[1] For further information on the 2014, 2020 Position Paper and the 2019 Consultation Paper, please refer to chapter 4, Section II. Furthermore, for an analysis into the crypto asset definition, as illustrated by the various policy papers, please refer to chapter 2, Section II.

[2] For an analysis into the crypto asset definition, as illustrated by the various policy papers, please refer to chapter 2, Section III, Sub-Section a.

[3] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group *Consultation Paper on Policy Proposals for Crypto* (2019) at 1.2.

- There are still no regulations for crypto assets.
- Crypto assets may expose consumers to financial and consumer risks.
- The popularity of crypto assets.
- These factors needed to be taken into account when formulating regulation for crypto assets. In recognising the need for regulation, the 2019 Consultation Paper identified the following case studies that were used to formulate crypto asset regulation:[4]
- Purchasing and selling of crypto assets;
- Payments made via crypto assets;
- Capital raising done through initial coin offerings (ICO);
- Crypto asset derivatives and funds; and
- Market provisioning of crypto assets.

These case studies were used to assist in formulating what regulations would be needed for crypto assets. However, the 2019 Consultation Paper placed an emphasis on only two of these case studies, being the purchasing and selling of crypto assets, and payments made via crypto assets.[5]

By focussing on these two case studies, it would enable the regulatory bodies, through the 2019 Consultation Paper to further expand on the concept of crypto assets and provide greater understanding as well as development into existing regulatory approaches and provide recommendations as to how crypto assets can be regulated.[6]

Following the 2014 Position Paper, and the 2019 Consultation Paper, the IFWG CARWG published the 2020 Position Paper, which further built on the knowledge and information given to regulatory bodies by the 2019 Consultation Paper and 2014 Position paper. In addition to further expanding the viewpoints of these past papers, the 2020 Position Paper also confirmed the information found in both these papers. The 2020 Position Paper, also further improved on, the definition of a crypto asset,[7] as illustrated in chapter 2, with cryptocurrency forming a subset of a crypto asset. This improved definition helped to further show the understanding of the regulatory bodies in relation to crypto assets.[8] The 2020 Position Paper acknowledges that crypto assets require regulation, and by analysing existing cases in relation to crypto assets, policies can be formulated which would emphasise the certainty of regulations.[9]

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[4] Ibid at 1.3.1.
[5] Ibid at 1.4.3.
[6] Ibid at 1.4.1.
[7] The collective term of crypto asset was further utilised in the 2020 Position Paper.
[8] For an analysis into the crypto asset definition, as illustrated by the various policy papers, please refer to chapter 2, Section III, Sub-Section a.
[9] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper on *Crypto Assets* (2020) at 1.2.2.

In realising the need for regulation, this position paper analysed crypto assets in relation to the economy. This is in stark contrast to the 2014 Position Paper which looked at crypto assets from a purely technological perspective, where it aimed to provide a more informative approach towards how crypto assets should be understood. The 2019 Consultation Paper redefined the understanding, and developed the term crypto asset, which is to be applied when dealing with this technology in South Africa. The 2019 Consultation paper did deal to an extent with the economic impact crypto assets have in South Africa. Hence it can be said that the 2019 Consultation Paper served as a 'bridge' in the understandings of crypto asset between 2014 and 2020, allowing a more detailed analysis as to how regulations can be developed, through the recommendations made in the 2020 Position Paper.[10]

The 2020 Position Paper made use of the same case studies[11] found within the 2019 Consultation Paper. However, unlike the 2019 Consultation Paper that only focussed on two cases,[12] the 2020 Position Paper focused on analysing a much wider variety of case-study examples.[13]

Therefore, it can be noted that the purpose of this chapter would be to provide an analysis into the findings these policy papers have made thus far. Furthermore, the collective term 'crypto asset' will be utilised in this chapter's analysis of these papers, as cryptocurrency is a subset of crypto asset.

II. 2014 POSITION PAPER

Chapter 2[14] provided a foundation in determining the definition of crypto assets. Although defining crypto assets is important—especially in understanding and distinguishing crypto assets from other virtual currencies—the focal point of this position paper was to highlight the risks posed to consumers who use crypto assets. The possible reason for merely focussing on the risks crypto assets posed to consumers can be attributed to the novelty of this technology at that particular time.

Within this paper the following risks posed to consumers who use crypto assets were identified:[15]

- Payment systems and payment service providers;
- Price Stability;

[10] Ibid at 1.3.2.

[11] The case studies include:

- Purchasing and selling of crypto assets;
- Payments made via crypto assets;
- Capital raising done through initial coin offerings (ICO);
- Crypto asset derivatives and funds; and
- Market provisioning of crypto assets.

[12] The 2019 Consultation Paper only focused on looking at the purchasing/selling and payments cases when evaluating crypto assets.

[13] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group op cit note 9 at 1.3.2.

[14] For an analysis into the crypto asset definition, as illustrated by the various policy papers, please refer to chapter 2, Section II.

[15] South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* (2014) at 4.

- Financial Stability;
- Money laundering and financing of terrorism;
- Consumer risk; and
- Circumvention of exchange control regulations.

Through highlighting the relevant risks, the 2014 Position Paper provided an understanding, that due to the unregulated nature of crypto assets, it would be able to flout conventional financial regulations. The reason for this stems from the fact that many laws that are put into place to mitigate the risks as mentioned above, pre-dates the creation of crypto assets. Furthermore, many of these regulations primarily regulate the concept of legal tender. Crypto assets do not fall within the ambit of what is considered legal tender.[16]

Hence, the 2014 Position Paper, in addition to conceptualising a definition for crypto assets, provided an analysis of the risks associated with crypto assets. These risks will be further analysed below.

a) Payment Systems & Payment Service Providers

It must further be noted that for a robust and effective financial system, a payment system is integral. Due to ongoing technological improvements in the financial sector, legislation regulating payment systems are required to adapt to these technological changes, whilst preserving the principles of the payment system. Hence, due to a crypto asset's underlying technology, namely blockchain,[17] it allows for crypto assets to function as a form of a payment system.[18]

By looking at the first risk, it can be said that through the 2014 Position Paper, crypto assets tend to challenge payment systems and service providers, with the possibility of being illiquid.[19] This results in service providers not being able to exchange crypto assets into fiat currency quickly and efficiently.[20]

Although crypto asset transactions may be quick, fast, and relatively inexpensive to process, the problem that occurs with the use of crypto assets, is when there is an exchange between fiat currency/legal tenders and crypto assets, as there may be 'a destabilising effect on the stability of the

[16] For an analysis into the crypto asset definition, as illustrated by the various policy papers, please refer to chapter 2, Section II, Sub-Section a.
[17] See chapter 2, Section III, Sub-Section c for an explanation on blockchain and the underlying technology of a crypto asset.
[18] L Sadhaseevan *The Regulation of Crypto Currency in The Context Of South Africa's Financial Sector* UKZN (2020) at 45; See also: R Sharrock *The Law of Banking and Payment in South Africa* (2016) at 78; J Maphosa 'Banking and Finance in Africa: Payment system regulations' (2017) 17 *Without Prejudice* 10 at 32; R Ali, R Clews, J Southgate 'Innovations in payment technologies and the emergence of digital currencies' *Bank of England* 2014 at 264, *available at www.bankofengland.co.uk/quarterly-bulletin/2014/q3,* accessed on 10 December 2020.
[19] According to Websters dictionary, illiquid refers to when an asset is not easy to sell or exchange for legal tender.
[20] South African Reserve Bank National Payment System Department op cit note 15 at 4.3.1.

payment system',[21] due to the illiquid nature of crypto assets. This illiquid nature can be attributed to the volatility associated with crypto assets.[22]

Furthermore, it must be noted that in terms of the National Payment System Department, payment systems in South Africa are based on cash and non-cash payments.[23] In respect of cash, this refers to legal tender as defined by the SARB Act 90 of 1989.[24]

Furthermore, crypto assets are not considered as a non-cash alternative. Non-cash alternatives refer to EFT's as well as e-money, credit and debit cards.[25]

Hence, in terms of the National Payment System of South Africa, crypto assets do not fall within the meaning of cash and non-cash payments and is therefore not formally recognised by the National Payment System of South Africa. Therefore, should merchants accept the payment for goods and services in terms of crypto assets, they would be doing so at their own discretion.

b) Price Stability

By looking at the risk of price stability in terms of crypto assets, SARB looked at the risk crypto assets may have on legal tender. This risk occurs due to the fact that there may be more people adopting and using crypto assets, as opposed to legal tender that is associated with the Reserve Bank. This may result in less demand for legal tender, and more use of crypto assets, which is currently not regulated by SARB. The detrimental result this may have on an economy is that SARB may not be able to influence interest rates, which the population of South Africa is dependent on. The reason for this is because there will be greater use and transactions of crypto assets as opposed to legal tender.[26]

However, what must be noted, is that according to the 2014 Position Paper, the current use of crypto assets is not at a stage that can threaten the price stability within South Africa, but the risk of price stability is a risk that could materialise in the future if there are no means of regulation for the use of crypto assets within South Africa.[27]

Furthermore, what can also be observed about crypto assets is their inherent volatility. The price of Bitcoin is an illustration of the volatility associated with the price of cryptocurrencies.

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[21] Ibid.
[22] Ibid.
[23] South African Reserve Bank National Payment System Department *Payment, clearing, and settlement systems in South Africa* (2012) at 382.
[24] In terms of Section 14 of the SARB Act 90 of 1989, legal tender is seen as being any form of coins or bank notes issues by a bank.
[25] N Kaplanov 'Nerdy Money: Bitcoin, the Private Digital Currency, and the Case against its Regulation' (2012) 25 *Loyola Consumer Law Review* 111 at 124.
[26] South African Reserve Bank National Payment System Department op cit note 15 at 4.
[27] South African Reserve Bank National Payment System Department op cit note 15 at 4.3.2.

As noted by Baur and Dimpfl:

> …total market value reached a first high of 13.9 billion USD on 4 December. The market plummeted afterwards and reached its lowest level of 2.4 billion USD on 14 January 2015. Since the end of 2015, the value of Bitcoin has again been steadily increasing. This is a first indicator that Bitcoin markets are very volatile.[28]

In addition, it has been noted that the illiquid nature of a crypto assets also contributes to its inherent volatility. Consequently, the fact that the price of crypto assets such as Bitcoin fluctuate vastly, also contributes to the idea that crypto assets cannot function as legal tender.[29]

The volatility of crypto assets can also be illustrated through a practical event, namely the COVID-19 pandemic. Through the COVID-19 pandemic, international stock market performances were negatively affected and were perceived as being unpredictable.[30] However, in comparison to traditional stock markets, it was found that crypto assets posed a higher irregularity/instability, and were generally impacted greater by the pandemic in its early stages resulting in low prices.[31] However, upon world-wide lockdowns, it resulted in a demand for non-traditional forms of 'investment' in the form of crypto assets. This resulted in the stark increase in prices of crypto assets, such as Bitcoin, when compared to traditional stock markets and fiat currencies.[32] This example illustrates the volatility of cryptocurrencies.

c) Financial Stability

Looking at the risk of financial stability, SARB considered this as a risk due to the fact that crypto assets could influence or threaten the existing manner in which financial systems operate. Specifically, SARB made note of how crypto assets may impact payment systems in South Africa. As noted above, crypto assets are not recognised as an official method of payment and therefore contributes to the risk of financial instability. However, when crypto assets are relied upon by individuals, and are given in exchange for goods and services, it will allow users of crypto assets to circumvent payment system regulations, resulting in a detrimental effect to the circulation of money within the country.[33]

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[28] D Baur & T Dimpfl 'Realized Bitcoin Volatility' 2017 *SSRN Electronic Journal*.
[29] K Kopke 'How do you classify cryptocurrency as an investment?' (2018) 18 *Without Prejudice* 2; See also: 'What Causes Volatility in Bitcoin?' *FXCM*, available at: *https://www.fxcm.com/za/insights/what-causes-volatility-in-bitcoin/*, accessed on 3 February 2020; L Graham 'How Bitcoin Could Overcome Its Wild Reputation' *CNBC* 2017, available at*: https://www.cnbc.com/2017/09/21/bitcoin-volatility-how-digital-currency-can-overcome-wild-reputation.html*, accessed on 3 February 2020.
[30] P Takyi & Bentum-Ennin 'The impact of COVID-19 on stock market performance in Africa: A Bayesian structural time series approach' 2020 *Journal of Economics and Business*.
[31] Demir *et al* 'The Relationship Between Cryptocurrencies and COVID-19 Pandemic' (2020) 10 *Eurasian Econ Rev* at 359-360.
[32] Ibid.
[33] Ibid at 4.3.6.

d) Money Laundering & Financing of Terrorism

Looking beyond the financial system, the risk of money laundering and financing of terrorism originates from the characteristics of crypto asset, namely it is anonymous and decentralised, resulting in no financial body being able to control it. By having no direct link to a financial body, it could result in crypto asset transactions flouting conventional laws put into place to prevent money laundering and financing terrorism. Many regulations to prevent money laundering, such as Exchange Control Regulations and the Financial Intelligence Centre Act 38 of 2001(FICA) pre-date the introduction of crypto assets. Further analysis of these regulations will be explored in chapter 4.[34]

e) Consumer Risk

SARB further highlights the risk posed to consumers by using crypto assets. This risk exists on the basis that crypto assets are unregulated. By virtue of being unregulated, it allows users of crypto assets to not be afforded any protection, should they experience any consumer risks such as fraudulent transactions, or errors in transactions. Furthermore, by linking the risk of financial stability to consumer risk, it can be said that due to the volatility of crypto assets, it may result in users of crypto assets experiencing considerable losses financially. Furthermore, there is a lack of insurance regulations and consumer protection afforded to users of crypto assets, in the event their service provider fails to process a transaction or their accounts become inactive. All of these risks, illustrate the little protection afforded to consumers.[35]

f) Circumvention of Exchange Control Regulations

Lastly, due to cryptocurrencies' relatively anonymous and decentralised nature, it allows crypto assets to flout exchange control regulations put into place to protect investors as well as prevent the 'loss of foreign currency resources through the transfer abroad of real or financial capital assets held in RSA'.[36]

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[34] Ibid at 4.3.3

[35] Ibid; See also: However, what must be noted in terms of this risk is that as of 2020, consumer protection laws in terms of the Consumer Protection Act 68 of 2008 will apply to an individual who is buying or selling a crypto asset through a registered CASP. A CASP refers to a crypto service provider, who facilitate transactions on behalf of crypt asset users within South Africa. An example of a CASP includes Luno. Further discussion of CASPs will be followed in this chapter. Due to the fact that a CASP offers a service to the consumer in the form of a crypto asset exchange, crypto asset storage or crypto asset transaction, 'a consumer is entitled to, just and reasonable terms and conditions and may not suffer prejudice in the form of extortionist agreements.' 'The regulatory status quo of cryptocurrency exchanges' *Go Legal* 2019, available at: *https://www.golegal.co.za/cryptocurrency-exchanges-regulatory*, accessed on 10 December 2020; See also: Consumer Protection Act 68 of 2008, Part G; South African Reserve Bank National Payment System Department op cit note 15 at 4.3.4.

[36] South African Reserve Bank National Payment System Department op cit note 15 at 4.3.5.

In terms of this, since the banking sector within South Africa has no control or authority over crypto assets, the movement of crypto assets are not subjected to the checks and balances that are provided for by banks for the movement of foreign currency. Furthermore, due to the characteristics and nature of crypto assets, the Exchange Control Regulations (to be further discussed in chapter 4) does not make provision for crypto assets within its purpose. Hence, the movement of crypto assets transactions will not be regulated by the Exchange Control Regulations.[37]

Hence, through the analysis of the 2014 Position Paper, it can be seen that this paper merely provided an understanding to the underlying nature of a crypto assets. However, it must be noted that at the time this position paper was published, crypto assets were still referred to as DCVC's or virtual currencies/cryptocurrencies, as opposed to 'crypto asset' which is a collective term that encompasses cryptocurrency.

Furthermore, it can be noted that SARB does not view crypto assets as a legal tender. This is detrimental to understand, as many regulations, both in terms of the financial and market sector have laws that regulate legal tenders. Hence, through SARB's definition, many regulations would simply not apply to crypto assets. This therefore results in various risks been identified by SARB. These risks are associated with individuals who engage in crypto asset transactions. In addition to highlighting various risks, it must be acknowledged that this position paper does not provide any recommendations to combat these risks. Furthermore, due to many regulations pre-dating the conception of crypto assets, these regulations do not include crypto assets within their ambit.

Consequently, it can be noted that this position paper provides an overview to an otherwise unknown subject at the time. It must be emphasised that through this position paper, it provided the stance in relation to crypto assets, SARB applied in 2014, until the 2019 Consultation Paper was published.

This stance emphasised that crypto assets are not illegal but any crypto asset transactions entered into would be done by the sole discretion of the individual who may bear the risk.

III. 2019 CONSULTATION PAPER

The 2019 Consultation Paper paid particular focus to the risks as mentioned in the 2014 Position Paper. These risks were used to illustrate the pitfalls of having crypto assets unregulated. This policy paper further made use of the term crypto asset as opposed to cryptocurrency.

[37] Ibid.

The 2019 Consultation Paper identified that crypto assets may be purchased or sold through a crypto trading platform, crypto asset vending machines, transactions between individuals who hold crypto assets or crypto asset mining.[38]

It was further acknowledged in the 2019 Consultation Paper, that there are no regulations to monitor and ensure the legality of purchasing and selling of crypto assets. In addition, it was identified that there is no established standard or rules that govern these transactions, which could result in circumvention of Exchange Control Regulations. Furthermore, the tracking of these transactions may be difficult as it is separate to the flow of funds relating to fiat currencies traditionally monitored by financial institutions.[39]

Consequently, crypto asset trading platforms and sellers may not have adequate consumer protection mechanisms to protect the consumer, should they engage with crypto asset trades, or alternatively experience fraud or theft of their respective crypto assets.[40]

Furthermore, the 2019 Consultation Paper identified that by virtue of the crypto asset market not being regulated, it allows individuals to manipulate the market to the uninformed consumer, and thereby making profits through undesirable methods.[41]

The 2019 Consultation Paper further explained the manner in which crypto assets may be utilised for payments. This extended on the knowledge found within the 2014 Position Paper, where crypto assets posed a risk to the payment system. The 2019 Consultation Paper further echoed the sentiment of the 2014 Position Paper, namely, that using crypto assets as a means of payment is at the sole discretion of merchants and consumers.[42]

In terms of using crypto assets as a payment system, it was identified that in addition to circumventing payment systems due to non-regulation, crypto assets create a parallel payment system

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[38] A trading platform, refers to form of decentralised exchange where crypto assets can be traded freely between users. This exchange functions through artificial intelligence. Through artificial intelligence, the exchange will facilitate trades between crypto asset users without any assistance or intervention from a third party, hence fulfilling the crypto asset characteristic of being decentralised. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 8; See also: 'What is a cryptocurrency exchange and how do they work' *Coin Insider* 2020, available at: *https://www.coininsider.com/cryptocurrency-exchanges/*, accessed on 10 December 2020.

[39] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 4.2.

[40] These risks can further be highlighted by a practical example. In South Africa, a company known as Vaultage Solutions provided crypto asset services, in terms of trading, investing through crypto mining, and crypto asset deposits. A minimum deposit of $50 was required to become a Vaultage Solutions client. A total of $13.35 million was invested by 2000 investors with the said company. However, the CEO of the company ceased communication with the company's investors and claimed bankruptcy based on poor performing markets. The invested money was 'lost', resulting in innocent consumers losing their money to a fraudulent scheme. This practical example illustrates that through a lack of regulation, individuals are able to exploit the financial system on the pretences of dealing with crypto assets. T Zimwara 'South African Investors to Lose $13 Million as Bitcoin Scammer Declared Bankrupt' *Bitcoin* 2020, available at: *https://news.bitcoin.com/south-african-investors-lose-13-million-bitcoin-scammer-bankrupt/,* accessed on 10 December 2020.

[41] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 4.2.

[42] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 3.2 and 4.2.

that could compete and reduce the function and efficiency of the national payment system. Furthermore, as mentioned above, there is a lack of consumer protection when crypto assets are utilised to pay for goods or services. Hence, when a transaction is made by mistake or if there are any errors, there are no consumer protections currently available to protect the consumer, apart from contractual and common law remedies.[43]

Contrasting the 2014 Position Paper however, the 2019 Consultation Paper provided benefits in relation to the risks. The benefits for purchasing/selling of crypto assets were identified as showing that crypto assets help to diversify investments that are not linked to a country's risk. Furthermore, its anonymity makes it appealing for individuals to engage in the purchasing and selling of crypto assets.[44] In terms of utilising crypto assets as a form of payment, the benefit associated is that it may lower the general transactional cost of a transaction, and in line with a crypto asset's characteristics provide for faster, and safer transactions both locally and internationally, when compared to traditional financial institutions.[45]

Hence, it can be noted that in addition to identifying and confirming the risks found within the 2014 Position Paper, the Consultation Paper also provides a balance by identifying relevant benefits that can be associated with the use of crypto assets.

The 2019 Consultation Paper focused on providing recommendations based on risks that have already materialised. Such risks that are identified to have materialised include: [46]

- Money laundering;
- Funding of terrorism;
- Exchange control circumvention;
- Tax evasion;
- Market integrity;
- Illicit financial flows.

In providing recommendations for the materialised risks, the 2019 Consultation Paper primarily provides approaches that can adopted to achieve the recommendations set out by the FATF in terms of AML/CFT.[47]

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[43] Ibid at 4.2.

[44] Ibid at 4.3; See also: For a greater understanding of risks and benefits of crypto assets, the following article may be relied upon: J Lee and F Lheureux 'A Regulatory Framework for Cryptocurrency' 2020 *SSRN Electronic Journal*.

[45] Ibid.

[46] D Geral & B Tibane 'South Africa Stepping Up Gear' *IFLR* 2019, available at: *https://www.iflr.com/article/b1lmxcdn48fnkf/south-africa-stepping-up-a-gear*, accessed on 19 September 2020; See also: E Reddy & V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies '(2019) 31 SA Mercantile Law Journal at 1-28; Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 5.2.

[47] Geral & Tibane op cit note 46; See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 5.3.2.

Currently, South Africa and its relevant regulatory bodies have merely released recommendations as to how crypto assets should be regulated. However, no regulation has been established by SARB or IFWG CARWG. This fact can be supported by the SARB 2014 Position Paper. These publications merely provided a recommendation and informed the public about crypto assets. The 2019 Consultation Paper proposes that in order to regulate crypto assets there needs to be guidance as to how crypto assets may be used and limited through regulation. By virtue of having some form of regulation, it will allow regulatory bodies to provide requirements to be followed when crypto assets are utilised without the need of 'formal authorisation'.[48]

Hence, this 2019 Consultation Paper, and FATF recommendations, provided that regulatory bodies in South Africa would need to provide stricter requirements in relation to crypto assets. FATF included both virtual assets and virtual asset service providers within its glossary of definitions. Therefore, in terms of South Africa, all CASPs—who are considered to fall within the ambit of a virtual asset service provider definition are also required to comply with the FATF recommendations. These recommendations are explicitly aimed at preventing AML/CFT.[49]

In ensuring the FATF recommendations are met, this 2019 Consultation Paper makes the proposal that crypto assets should not be considered as a legal tender or e-money within South Africa—largely confirming definitions found in the 2014 Position Paper. However, by virtue of the umbrella term 'crypto assets' being introduced in the 2019 Consultation Paper, it does contrast the view of the 2014 Position Paper with regards to not classifying a crypto asset as a security. By virtue of security tokens falling within the ambit of a crypto asset, it can be inferred that a crypto asset can be considered a security.[50]

However, no further comment was given with regards to this aspect in the 2019 Consultation Paper. Furthermore, the paper suggests that a regulatory framework for crypto assets be implemented and developed across three phases, whereby the first phase provides for CASPs to be registered. The second phase proposed, reviews existing legislation to see if the legislation is applicable to the regulation of crypto assets. Should the legislation not be applicable to crypto assets, then the said legislation may be amended to include crypto assets within its scope. However, should the legislation not be able to be

[48] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 5.3.2; See also: J Lansky 'Possible State Approaches to Cryptocurrencies' (2018) 8 *Journal of Systems Integration*; for an in-depth explanation as to how approaches used by various countries around the world relating to crypto assets are classified.

[49] Recommendations for the FATF can be found at: *http://www.fatfgafi.org/publications/fatfrecommendations/documents/regulation-virtual-assets.html;* See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 5.3.2.

[50] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 8, See also: D Geral op cit note 46; See also: chapter 2 for a definition of crypto assets; K Kopke 'How do you classify cryptocurrency as an investment?' op cit note 29.

amended then new regulations will be formulated. The third phase will involve a registration of all entities involved in crypto asset activities.[51] These entities may be classified as being:[52]

- Trading platforms that facilitate the purchasing and selling of crypto assets, or the exchange of crypto assets into legal tender, other crypto assets or value of other crypto assets. It's important to note that crypto asset vending machines will be considered as being able to facilitate these activities.
- Digital wallet providers for the storage of crypto assets.
- Crypto asset safe custody.
- Payment service providers who accept crypto assets as a means of exchange.

In addition to these various phases, it is further proposed that in order to achieve the recommendations of the FATF, these crypto asset entities will be required to comply with the FICA in order to achieve AML/CFT requirements.[53]

Hence, FICA will need to be amended to include CASPs/crypto asset entities as within the definition of an 'accountable institution' as found within Schedule 1 of the FICA. By virtue of falling within the ambit of the FICA, all CASPs/crypto asset entities will be required to comply with FICA and register with Financial Intelligence Centre (FIC). As a result of being registered in terms of the FICA, all CASPs will then be required to comply with the act, which provides that all CASPs will have to ensure the following:[54]

- Duty to identify clients.[55]
- Duty to keep records of the client.[56]
- Reporting Duties and access to client information to be given to FIC.[57]
- Measures to promote compliance of the act.[58]
- In addition, it was recommended that entities report individuals who make cash transactions of R25000 or more and any control of property that is related to terrorist activities.[59]

[51] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 8; See also: D Geral op cit note 46.
[52] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 8 at 8.8.
[53] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 8.9.
[54] Chapter 3 of the Financial Intelligence Centre Act 38 of 2001. This chapter of the FICA employs control measures in place to prevent money laundering and the financing of terrorism to occur.
[55] Sections 21 of the Financial Intelligence Centre Act 38 of 2001.
[56] Sections 22 to Section 26 of the Financial Intelligence Centre Act 38 of 2001.
[57] Sections 27 to Section 41 of the Financial Intelligence Centre Act 38 of 2001.
[58] Sections 42 to Section 43 of the Financial Intelligence Centre Act 38 of 2001.
[59] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3.

Should CASPs/crypto asset entities not comply with FICA, the relevant offences and penalties implemented by the FICA will be used in cases of non-compliance by CASPs.[60]

In addition to these proposals, this Consultation Paper further proposes that South Africa should continue to monitor the use of crypto assets. This monitoring will be accomplished through ensuring that CASPs as well as crypto asset vending machines within South Africa report the flow of crypto assets that they transact and store, monitoring payment systems, and lastly monitoring the general market and market capitalisation of crypto assets.[61]

Therefore, through this 2019 Consultation Paper, it can be understood that it aims to build on the information published in the 2014 Position Paper. However, in addition to confirming and building on the information found within the 2014 Position Paper, the 2019 Consultation Paper provides a more functional approach, through its various proposals towards the regulation of crypto assets. What can be deduced is that the proposals offered by this paper aim to ensure that AML/CFT is achieved. Through this paper, the proposals target CASPs, that will be handling crypto asset transactions on behalf of clients.

Hence, it provides a method to ensure there is 'limited regulation' of crypto assets. In addition to these proposals, one of the key takeaways of the 2019 Consultation Paper is that it further developed the understanding and introduced the collective term of crypto assets, which encapsulates various categories of crypto assets, one of them being cryptocurrency.

IV. 2020 IFWG CARWG POSITION PAPER

The focal point of this position paper is to highlight the various recommendations the IFWG and CARWG has developed, taking into account the past position papers and the dynamic nature of crypto assets. In making recommendations, the 2020 Position Paper took into account both existing legal frameworks and legal frameworks that are to be developed.[62]

Consequently, this particular position paper provides in total, thirty recommendations for the regulation of crypto assets within South Africa. These recommendations have been divided accordingly in relation to the case studies utilised by this 2020 Position Paper. Recommendations one to eight relate to overall recommendations made, whilst recommendations nine to thirty represent recommendations made according to the case studies.

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[60] Chapter 4, Sections 46 to 71 of the Financial Intelligence Centre Act 38 of 2001; See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3.

[61] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 8.10.

[62] Legal frameworks that are under development include the Conduct of Financial Institutions Bill. More information of this bill will be provided in chapter 4.

In terms of the overall recommendations, these essentially highlight the need for CASPs to conduct their services within the ambit of the FATF recommendations,[63] which deal with 'virtual assets' and 'virtual service providers'.[64] This recommendation is largely in line with the proposal found in the 2019 Consultation Paper, which also required CASPs to be included as an 'accountable institution' in Schedule 1 of the FICA. Furthermore, the 2019 Consultation Paper referred to the classification of CASPs.[65]

Contrasting the 2019 Consultation Paper, it can be noted that the classification of CASPs has been expanded to six categories within the 2020 Position Paper. The 2020 Position Paper added the following categories:[66]

- Issuers of crypto asset tokens: In terms of this entity, it makes provision for those who issue ICO's, any financial services related to the offer or sale of crypto assets, as well as the issue of both stable coins and global stable coins.
- Investment/derivative service providers where crypto assets are the underlying asset.

It should be further observed that, in relation to the definition discussed above, the existing definition of a crypto asset provided by the 2020 Position Paper does not provide for Stablecoins within its definition due to the fact that when the term 'crypto asset' was formulated by the IFWG CARWG, it pre-existed the concept of Stablecoins.[67] However by a simple reading of the CASP entities found within the 2020 Position Paper, it shows that the IFWG and CARWG respectively do recognise Stablecoins as a crypto asset token, as it is included within CASP entities who issue crypto asset tokens.[68]

In recommending that CASPs conform with FATF recommendations, the 2020 Position Paper proposes that in terms of the FICA, CASPs should be included within the scope of an 'accountable

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[63] The FATF recommendations are global standards that are recognised and endorsed for the prevention of financing terrorism and money laundering.

[64] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.1, Recommendation 1.

[65] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group *Consultation Paper on Policy Proposals* op cit note 3 at 8.8, the entities that classify as a CASP according to the 2019 Consultation paper include:

- Trading platforms that facilitate the purchasing and selling of crypto assets, or the exchange of crypto assets into legal tender, other crypto assets or value of other crypto assets. It's important to note that crypto asset vending machines will be considered as being able to facilitate these activities.
- Digital wallet providers for the storage of crypto assets.
- Crypto asset safe custody.
- Payment service providers who accept crypto assets as a means of exchange.

[66] It must be noted that the classification of CASP entities, as recommended by the 2020 Position Paper is in line with Recommendation 15 of the FATF, which details the categories of CASPs; See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.1.1; See also: 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' *IR Global* 2020, available at: *https://www.irglobal.com/article/crypto-assets-in-south-africas-financial-regulatory-landscape-the-latestdevelopments-2/*, accessed on 10 December 2020.

[67] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 2; See also: Section III, section a for a discussion on Stablecoins.

[68] Refer to Section IV, Sub-Section b of chapter 3 for a discussion on the definition of a crypto asset found within the 2020 Position Paper.

institution' as found in Schedule 1 of the FICA. The result of this inclusion would allow FICA to be applied in relation to CASPs, hence, all CASPs will have to ensure compliance with this act. In addition, it is also provided that through the FICA, the FIC would ensure management of these CASPs, through compliance with the FICA and should there be non-compliance, remedial actions as highlighted by the FICA will be utilised. This would ensure that AML/CFT requirements are adhered, in line with the FATF recommendations.[69]

In addition to the compliance required with the FICA, CASPs will be required to comply with Recommendation 16 of the FATF Recommendations.[70] Recommendation 16 provides a 'travel rule' for all CASPs. This 'travel rule' makes it compulsory for the sender CASP and recipient CASP, who engage in a transaction between themselves involving crypto assets to reserve and retain information relating to the transactions and share this information with relevant regulatory bodies when required This recommendation is imperative in terms of AML/CFT.[71]

Furthermore, the sender CASP is required to share and send personally identifiable information to their recipient CASP.[72] This recommendation helps to increase confidence in relevant stakeholders when dealing with crypto assets and protect consumers from any forms of scams, or hacking of their crypto asset wallets.[73]

Following these recommendations, the 2020 Position Paper also recommends and confirms that a crypto asset monitoring programme should be established, based on the proposals of the 2019 Consultation Paper, that proposed five different methods of monitoring crypto assets, as noted earlier in this chapter.[74] In addition, the 2020 Position Paper also recommends that crypto assets should not be considered as legal tender or e-money, confirming the perspectives of both the 2014 Position Paper and 2019 Consultation Paper.[75]

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[69] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.2, Recommendation 2 & at 8.4.3, Recommendation 3, at 9.1.2.11, recommendation 19. In terms of Recommendation 2 and 3, it can be noted that this recommendation ensures that all sections of the FICA are to be applied to CASPS. This is further discussed earlier in this chapter, within the analysis of the 2019 Consultation Paper.

[70] In addition, all requirements of the FATF Recommendations are applicable to CASPs and need to be complied with. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.1.2.12, Recommendation 20.

[71] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.2.2, Recommendation 2; See also: for further reading: 'South Africa's Crypto Asset Service Provider (CASP) Regulation To Align with FATF Standards and Travel Rule' *Sygna* 2020, available at: *https://www.sygna.io/blog/south-africas-crypto-asset-service-providers-casps-to-comply-with-fatfs-r-16-travel-rule/,* accessed on 10 December 2020; 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' op cit note 66.

[72] Ibid.

[73] Ibid.

[74] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.4, Recommendation 4.

[75] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.5, Recommendation 5.

Another overall recommendation made by the 2020 Position Paper, looks at regulatory bodies such as SARB, the FSCA, National Payment System Department and the Prudential Authority considering appropriate policy in relation to crypto assets, and in the absence of such policy, regulatory bodies should not enter into crypto asset transactions. Hence, this recommendation shows that if a regulatory body does not have adequate policies and understanding to deal crypto assets, then these bodies should not utilise crypto assets in their respective markets.[76]

The 2020 Position Paper also recommended that the SARS provide a definition for crypto assets that is in line and harmonised with South African regulatory bodies. Currently, SARS recognises the subset of cryptocurrencies only, rather than the collective term 'crypto asset'. However, the Income Tax Act 58 of 1962 and the Value Added Tax Act 89 of 1991 makes direct reference to crypto assets within its wording. Furthermore, through the Draft Taxation Law Amendment Bill, as well as Value Added Tax Act, it also emphasised looking at crypto assets as a financial instrument.[77] Hence, through this recommendation the 2020 Policy Paper attempts to ensure that *all* regulatory bodies apply a unified definition for crypto assets.[78]

In addition to the recommendations discussed above, the 2020 Position Paper also provided recommendations for the case studies as identified in the 2019 Consultation Paper. The 2019 Consultation Paper merely provided recommendations to two case studies, namely being the purchasing and selling of crypto assets, and payments made via crypto assets.[79]

However, the 2020 Position Paper provides recommendations for all case studies.[80]

a) The Purchasing/Selling of Crypto Assets

This is one of the case studies that has been identified by the 2019 Consultation Paper as well as the 2020 Position Paper. By engaging in the purchasing and selling of crypto assets, it may result in a number

[76] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.6 and 8.4.7, Recommendation 6 and 7.

[77] Draft Taxation Laws Amendment Bill (Draft TLAB) (16 July 2018); See also: 'Cryptocurrency and Tax' *Bowmans* 2019, available at: *https://www.bowmanslaw.com/wp-content/uploads/2018/11/Session-3-Cryptocurrency-and-Tax.pdf*, accessed on 5 November 2020; R Basson 2020, 'An analysis of issues relating to the taxation of cryptocurrencies as financial instruments' (2020) 13 *Journal of Economic and Financial Sciences* 1 at 487

[78] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 8.4.8, Recommendation 8.

[79] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 3 at 1.4.3.

[80] Case studies include:

- Purchasing and selling of crypto assets;
- Payments made via crypto assets;
- Capital raising done through initial coin offerings (ICO);
- Crypto asset derivatives and funds; and
- Market provisioning of crypto assets.

Further discussion of how legislation and these case studies interact can be found in chapter 4.

of risks for the financial and market sector of South Africa as well as consumers themselves. Such risks can include:[81]

- Exchange control risks;
- Money laundering/Financing of terrorism;
- Operational risks; and
- Consumer market risks.

In identifying these risks, the 2020 Position Paper has proposed various recommendations to reduce or prevent these risks. One of these recommendations include recommending that crypto assets are considered as a financial service in terms of the regulatory framework found within the Twin peaks Model. Through this regime the 2020 Position Paper recommends that the Financial Sector Regulation Act 9 of 2017 (FSRA) be utilised, whereby in terms of this Act, the services of buying and selling crypto assets must be considered to be included within the definition of a 'financial service'.

Hence by virtue of the FSRA being relied upon, and the above services falling within the definition of financial services, it would allow the FSCA to be responsible for the licensing of purchases and sales of crypto assets, as well as creating and developing standards to be complied with by all CASPS. Furthermore, crypto assets must also be included in terms of licensing under the Conduct of Financial Institutions Bill (COFI Bill).[82]

In order to address cross-border transactions, the 2020 Position Paper recommends that SARB should take control of monitoring cross-border crypto asset transactions that occur. This control would be achieved through the Financial Surveillance Department (FinSurv) of the SARB, who would have both supervisory and regulatory responsibility to ensure the control.[83]

In summary, the 2020 Position Paper recommends that the Exchange Control Regulations be amended to encompass the meaning of crypto assets within the definition 'capital'. This would therefore allow the Exchange Control Regulations to be applicable towards crypto assets, and therefore allows crypto assets to be subjected to exchange control regulations. In addition, further amendment to the Exchange Control Regulations would be required in order to allow consumers to purchase crypto assets

[81] Refer to Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 4.4.1, for more information and explanation on these risks.

[82]The COFI Bill will further be explained in chapter 6. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.1.2.1 and 9.1.2.2, Recommendation 9 and 10; See also: 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' op cit note 66.

[83] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.1.2.4—9.1.2.10, Recommendations 12-18; See also: 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' op cit note 66. Recommendations twelve to eighteen detail the 2020 Position paper's stance as to how cross-border transactions can be amended to include crypto assets within its scope of regulation. Exchange Control Regulations will be further discussed in chapter 4.

within their single discretionary allowance/foreign capital allowance, as indicated within the regulations.[84]

It can also be noted that the 2020 Position Paper also recommends that the Authorised Dealers' manual be amended to include the reporting of crypto asset cross border transactions. Lastly, a recommendation is made to ensure that crypto asset trading platforms are considered to be an authorised dealer in respect to Exchange Control Regulations. The result of being an authorised dealer, would mean that crypto asset trading platforms would be required to report to the FinSurv.[85]

As it can be noted the recommendations from the 2020 Position Paper aim to ensure that crypto assets are defined and contained within Exchange Control Regulations. By virtue of this fact, it then allows crypto assets to be subjected to relevant exchange control regulations. Thereby, this would prevent irregular cross-border crypto asset transactions from occurring.

b) Payments made with Crypto Assets

The 2020 Position Paper acknowledges that the National Payment System Act 78 of 1998 (NPS Act) is under review. Due to the NPS Act being reviewed, it is recommended that the NPS Act therefore include the use of crypto assets as a payment system for domestic use. In addition to including crypto assets as a domestic payment system, the 2020 Position Paper recommends that a sandbox approach may be used to ensure that crypto assets are used within a regulated and controlled environment. This sandbox approach can best be described as an approach that determines the risks and benefits of using crypto assets as a form of a payment system.[86]

c) Initial Coin offerings

New companies may rely on alternate methods such as ICO's to raise capital.[87] However, this new form of capital raising is relatively unregulated, and will need to be contained within defined regulations. Hence, the 2020 Position Paper proposed that ICO's must be adjusted in a manner where it will fall under the regulation of 'over the counter' financial instruments. Furthermore, such tokens would therefore be regulated in terms of securities regulations found within the Financial markets Act 19 of 2012 (FMA). [88]

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[84] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.1.2.4—9.1.2.10, Recommendations 12-18; See also: 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' op cit note 66.

[85] Ibid.

[86] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.2.2.1, Recommendation 21; See also: 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' op cit note 66.

[87] As discussed earlier in this chapter and in chapter 2, Section IV, Sub-Section e.

[88] Over the counter financial instruments refer to securities that are traded through a person or form who are involved in the purchase or selling of securities on behalf of their respective clients, also known broker-dealer network as opposed to

In addition, it is also recommended that should an ICO be utilised for utility tokens, payment or exchanges, then such ICO's should be understood to constitute as a 'financial service', and therefore be regulated in terms of the FSRA, as well as being regarded as part of 'licensing' in terms of the COFI Bill, as mentioned above.[89]

Lastly, should a CASP issue tokens or provide financial services for the sale of a crypto asset in relation to ICO's, then relevant AML/CFT requirements must be followed and such a CASP must become an accountable institution as proposed earlier in this chapter. Such an accountable institution would be found within Schedule 1 of FICA, as recommended by the 2020 Position Paper.[90]

Hence, what can be observed of these recommendations for ICO's is that they directly relate to earlier recommendations made by the 2020 Position Paper. However, the recommendations vary based on the activity associated with the ICO. Hence if the ICO is being utilised as a utility token or is purchased—it is considered a Financial instrument and the FSRA in conjunction with the COFI Bill applies. However, if an ICO is being purchased or sold through a CASP by a consumer, then the FICA applies. If these two activities do not apply, then the relevant ICO will be considered to be regulated in terms of the FMA.

d) Crypto Asset Funds & Derivatives

The 2020 Position Paper recognises that various asset classes may be utilised by investment schemes and pensions, and therefore it is recommended that crypto asset be considered as an investment/derivative product.[91]

In recommending crypto assets as an alternate investment, it must be noted that the definition of a derivative investment found within the FMA should include crypto assets within its definition. As noted by the 2020 Position Paper, the definition of derivative investment is described as 'agnostic'. Hence, this can be inferred to mean the definition is vague, and as it stands, due to its vagueness can be interpreted to include crypto assets as an asset which is considered a derivative investment.[92]

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a centralised exchange. C Murphy 'Over the Counter (OTC)' *Investopedia* 2020, available at: *https://www.investopedia.com/terms/o/otc.asp,* accessed on 18 December 2020; See also: A Hayes 'What is a Broker Dealer?' *Investopedia* 2020, available at: *https://www.investopedia.com/terms/b/broker-dealer.asp*, accessed on 14 December 2020. Further discussion of the Financial Markets Act 19 of 2012 will be discussed in chapter 4. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.3.2.1, Recommendation 22; See also: 'Crypto Assets in South Africa's financial regulatory landscape – The latest developments' op cit note 66.

[89] For further information, refer to: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.3.2.3, Recommendation 23.

[90] [90] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.3.2.4, Recommendation 24, also refer to Recommendations 1, 2 and 3 of the 2020 Position Paper.

[91] A derivative product may refer to a product whose value is based on a primary product. For example, a particular products value may be derived from the price of gold.

[92] The Financial Market Act 19 of 2012 will further be analysed in chapter 4. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.4.1.1 and 9.4.1.2.

However, it is further noted that pooling of crypto assets results in having an alternative investment fund. Hence this would require licensing in terms of the COFI Bill. In addition to this, collective investment schemes cannot include crypto assets in its respective portfolios.

In relation to pension funds, the FSCA is required to determine whether crypto assets are an allowable asset to be utilised in terms of pensions.[93]

Furthermore, 'over the counter' instruments which are crypto assets need to be licensed in terms of the FSCA. In addition, derivative instruments that are crypto assets will need to be included in the framework relating to the FSCA, whereby the framework would provide requirements relating to settling a crypto asset derivative investment in legal tender.[94]

Lastly, any CASPS dealing with any investments/derivative investments in terms of crypto assets is required to conform with the relevant AML/CTF requirements found within the FICA.[95]

e) Crypto Asset Market Support Services

This case study merely refers to digital wallet services offered and custody safe services for the secure storage of crypto assets.[96]

Generally, CASPS will offer these types of services to consumers. Hence, it is recommended that in addition to the buying and selling of crypto assets, the storing of crypto assets using digital wallets or custody safes also be considered a 'financial service' in terms of the FSRA, and therefore a licensing activity in terms of the COFI Bill.[97]

Furthermore, by virtue of CASPS offering these services, they will be required to adhere to AML/CTF requirements in terms of the FICA.[98]

V. CONCLUSION

The 2014 Position Paper served as a foundation to provide the general public as well as regulatory bodies, with a basic understanding of what crypto assets are and the risks associated with the use of these crypto assets within South Africa. The general tone of the paper was merely to warn and educate citizens and regulatory bodies of crypto assets. This paper did not in any way ban the use of crypto assets nor did it recommend any legislative changes to enhance the regulation of crypto assets.

[93] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 9 at 9.4.2.1 and 9.4.2.2, Recommendations 25 and 26.
[94] Ibid at 9.4.2.3, Recommendation 27.
[95] Ibid at 9.4.2.4, Recommendation 28.
[96] Ibid at 9.5.2.1, Recommendation 29.
[97] Ibid.
[98] Ibid at 9.5.2.2, Recommendation 30.

However, the 2019 Consultation Paper was starkly different to the 2014 Position Paper. It confirmed various aspects of the 2014 Position Paper, but proceeded to build on the knowledge that had been acquired about crypto assets since the release of the 2014 Position Paper. This resulted in a more accurate term being introduced to describe this type of financial technology, i.e., crypto asset. This paper went on to further make various recommendations, namely detailing methods as to how crypto asset transactions and use in South Africa can comply with FATF recommendation on AML/CTF.

Lastly, the 2020 Position Paper provided recommendations on forming a regulatory framework that can assist to tackle the various case studies mentioned by the 2014 Position Paper and 2019 Consultation Paper. In addition to this, the recommendations ensured compliance with the FATF Recommendations. A regulatory framework addressing how CASPs would be regulated, AML/CTF adhered too, licensing regimes and Exchange Control Regulations were suggested.

Through these three papers, it provided a stance that has been developed through the years from a position paper that was merely a warning to consumers and regulatory bodies to one that offers a regulatory framework that can be adopted by regulatory body to instil confidence in financial institutions and all relevant stake holders through the regulation of crypto assets.

Various legislative acts were referenced in this chapter. These respective legislative acts will further be discussed in chapter 4, to determine whether recommendations from the position papers have been applied and how existing legislation is impacted by crypto assets.

It must however be noted that these policy papers do not constitute as regulation. At the time this dissertation was published, crypto assets still remain largely unregulated. These proposals however serve to provide regulatory with guidance and conditions as to how crypto asset regulations may be approached and developed.

CHAPTER 4

WHAT REGULATIONS ARE AVAILABLE TO REGULATE CRYPTO ASSETS

I. CHAPTER OVERVIEW

This chapter is going to provide an analysis into the relevant financial regulation required for the efficient regulation of crypto assets, namely cryptocurrencies. In the past, South Africa operated its financial regulation based on a single regulation policy, that could best be described as fragmented.[1] As with chapter 3, the collective term of crypto assets, which encompasses cryptocurrencies, will be used within this chapter, where relevant. Through the introduction of the Financial Sector Regulation Act 9 of 2017 (FSRA), South Africa's single regulation policy evolved into a two-tier approach known as the Twin Peaks model of regulation. The Twin Peaks model of regulation provides for the existence of the Prudential Authority (PA) and Financial Sector Conduct Authority (FSCA).[2]

It must be noted that there is not a single piece of legislation that can regulate the financial environment in relation to crypto assets. There are various pieces of legislation, and an analysis will be further conducted on legislation *relevant* to the regulation of cryptocurrencies. Therefore, in terms of the PA, the following Acts are of relevance in assessing crypto assets:

- Banks Act[3]
- South African Reserve Bank (SARB) Act[4]

Furthermore, in terms of the FSCA, the following Acts are of relevance with regards to crypto assets:

- FSRA[5]
- Financial Intelligence Centre Act (FICA)[6]
- Financial Advisory and Intermediary Services Act (FAIS) [7]
- Financial Markets Act (FMA)[8]

[1] The reason for the single regulation policy being fragmented is due to the fact that different regulators had control of and regulated different areas of the financial sector. U Ramracheya 'The Twin Peaks Model – A New approach' 18 (2018) *Without Prejudice* 8 at 18; See also: South African National Treasury *Policy Document: A safer financial sector to serve South Africa better* (2011) at 28; See also: A Viljoen, V Lalloo, S Bunge 'Financial Sector Regulation Act: Implementing Twin peaks and the impact on the industry' *Ernest and Young* 30 March 2018 at 2, *available at http: www.ey.com/ZA/en*, accessed on 18 January 2021.
[2] Ibid.
[3] Banks Act 94 of 1990.
[4] South African Reserve Bank Act 90 of 1989.
[5] Financial Services Regulation Act 9 of 2017.
[6] Financial Intelligence Centre Act 38 of 2001.
[7] Financial Advisory and Intermediary Services Act 37 of 2002.
[8] Financial Markets Act 19 of 2012.

In addition to the above, the Currency and Exchanges Act,[9] in conjunction with Currency and Exchanges Regulation, will be analysed to determine how cross-border transactions and off-shore accounts, in relation to crypto assets may be regulated.[10]

Therefore, this chapter will provide an analysis of the above legislation in relation to the use of crypto assets within South Africa, and a comment on its general applicability.

II. OVERVIEW OF REGULATORY AUTHORITITES

a) South African Reserve Bank (SARB)

SARB is the central bank of South Africa, that employs monetary policies to manage South Africa's inflation as well as provide a form of price stability to ensure economic growth. Furthermore, SARB is guided in terms of the Constitution,[11] and the SARB Act 90 of 1989.[12] SARB currently does not have legislation to regulate cryptocurrency within South Africa.[13]

The SARB identified the need to develop an understanding in relation to cryptocurrencies as well as a form of regulatory framework, to ensure that the financial sector of South Africa is not compromised through the use of cryptocurrencies.[14]

Therefore, in 2014, SARB, through the National Payment System Department (NPSD) published the 2014 Position Paper. Within this 2014 Position Paper, the stance of SARB in relation to cryptocurrencies is detailed, by looking at the general definition and understanding that is formulated by SARB in relation to cryptocurrencies, as well as the risks associated with the use of cryptocurrencies.

In the absence of legislation that comprehensively regulates cryptocurrencies in South Africa, the 2014 Position Paper assisted in indicating the intention and attitude of SARB towards the use and

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[9] Currency and Exchanges Act 9 of 1933.

[10] In addition to finance regulation and taxation, it must be noted that regulation of crypto assets beyond the finance scope has been advancing. An example of this can be found in the form of the Protection of Personal Information Act 4 of 2013 (POPI) refers to legislation that is used to protect private information of data sources. This particular regulation can also be applied to crypto assets, in terms of its technology (blockchain). By looking at POPI, as well as blockchain, it can be seen that both the legislation as well as technology looks at protecting information — POPI, through setting conditions for responsible parties that must be followed to ensure that information is protected and blockchain through encryption. Encryption refers to where information or data is converted to code to prevent unauthorised access. The data is therefore unrecognisable and can only be accessed by authorised parties. POPI must be considered and further analysed to determine whether the contents of this regulation are applicable to cryptocurrency transactions as well. For further reading please refer to: V Barapatre, 'How Blockchain Can Back POPI', *Gadget* 2018, available at: *https://www.gadget.co.za/how-blockchain-can-back-popi/*, accessed on: 20 April 2020; See also: '*Encryption' Tech Terms* 2014, available at: *https://techterms.com/definition/encryption.,* accessed on: 10 May 2020; for more insight on encryption.

[11] The South African Reserve Bank is guided in terms of Sections 223,224 and 225 of the Final Constitution.

[12] 'Mandate' *South African Reserve Bank*, available at: *https://www.resbank.co.za/AboutUs/Mandate/Pages/Mandate-Home.aspx*, accessed on 29 June 2020.

[13] Ibid.

[14] South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* (2014) at 4.

trade of cryptocurrency. The 2014 Position Paper[15] was SARB's first public pronouncement on cryptocurrency.[16]

b) Intergovernmental Fintech Working Group (IFWG)

The IFWG was established in 2016. The founding members of this group include the National Treasury, SARB, the Financial Sector Conduct Authority (FSCA), and Financial Intelligence Centre (FIC). Following the establishment of the group, regulators such as the National Credit Regulator, South African Revenue Service (SARS) and the Competition Commission also joined the IFWG. The IFWG's aim is to ensure regulators have an understanding of Fintech[17] and the effects Fintech has on the economy.[18]

Hence, it can be understood that the IFWG ensures that regulators have a common understanding with regards to Fintech.[19]

c) Crypto Assets Regulatory Working Group (CARWG)

Following the establishment of the IFWG, the CARWG was further established in 2018 to oversee the position of cryptocurrency within South Africa. The objective of the CARWG is to advise on regulations that may be applicable to regulate cryptocurrency. This working group is comprised of the IFWG and SARS.[20]

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[15] The 2014 Position Paper is discussed in greater detail in chapter 3 of this Dissertation.

[16] South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* (2014).

[17] Fintech is the shortened form of financial technology and it refers to technology that is used within the financial industry to automate and deliver financial services. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper on *Crypto Assets* (2020) at 4.

[18] Ibid.

[19] Furthermore, the IFWG achieves this aim by utilising an 'Innovation Hub'. This Innovation Hub provides for regulators to research, test potential recommendations and ensure the development and understanding of Fintech within South Africa. Through the Innovation Hub, the regulators that form part of the IFWG, integrate their understandings and ideas collectively to develop prospective solutions to achieve the aims of the IFWG. A Itzikowitz & I Meiring, 'Blockchain and Cryptocurrency Regulations 2020 South Africa', *Global Legal Insights* 2020, available at: *https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/south-africa,* accessed on: 12 April 2020; See also: For further reading on the IFWG, please refer to the IFWG Innovation Hub FAQS, available at: *https://www.resbank.co.za/content/dam/sarb/quick-links/fintech/IFWG%20Frequently%20asked%20questions%20-%20updated.pdf*.

[20] SARS refers to the revenue service of South Africa. Through its interpretation of cryptocurrency, it enables to determine the manner in which cryptocurrency may be taxed. Furthermore, SARS provides an alternate perspective to the SARB and respective working group position papers; See also: 'Sars stance on the tax treatment of cryptocurrencies' *SARS* 6 April 2018, available at: *https://www.sars.gov.za/Media/MediaReleases/Pages/6-April-2018---SARS-stance-on-the-tax-treatment-of-cryptocurrencies-.aspx*, accessed on 24 May 2020; See also: A Itzikowitz & I Meiring 'South Africa: Blockchain and Cryptocurrency Regulations 2020 South Africa' op cit note 19.

The CARWG utilises a functional approach[21] in developing a regulatory foundation for crypto currencies in South Africa.[22] The functional approach is utilised in conjunction with various case studies that is applied by the CARWG. These case studies narrowed the scope in which the CARWG developed its regulatory response, however there are various other case studies (which are not utilised by the CARWG) that can be used to develop a regulatory response and provide greater understanding towards the general risk associated with dealing with cryptocurrencies.[23]

Through this working group, and in conjunction with the IFWG, a consultation paper was released in 2019, and a position paper released in 2020, building on the intentions and perspective of the 2014 SARB Position Paper.

The 2019 Consultation Paper[24] focussed on the development of regulatory proposals, rather than highlighting and merely providing an understanding to the risks and technology underpinning cryptocurrencies. In doing so, this consultation paper identified the potential uses that cryptocurrencies may be utilised for and also the manner in which South Africa can promote anti-money laundering/counter terrorism financing (AML/CTF) recommendations, as proposed by the Financial Action Task Force (FATF),[25] through the use of cryptocurrencies.[26]

The 2020 Position Paper[27] built on the information provided by both the 2014 Position Paper and 2019 Consultation Paper. The 2020 Position Paper provided recommendations for the development of a cryptocurrency regulatory framework within South Africa. This regulatory framework will ensure AML/CFT recommendations are followed—much like the suggestions highlighted in the 2019 Consultation Paper. Furthermore, the 2020 Position Paper also provided a greater understanding of

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[21] The functional approach is utilised in conjunction by various case studies that is applied by the CARWG. These case studies narrowed the scope in which the CARWG developed its regulatory response, however there are various other case studies (which are not utilised by the CARWG) that can be used to developed a regulatory response and provide greater understanding towards the general risk associated with dealing with cryptocurrencies.

[22] A Itzikowitz & I Meiring 'South Africa: Blockchain and Cryptocurrency Regulations 2019' op cit note 19.

[23] Case studies utilised by the CARWG include:

- Purchase and sale of crypto currencies;
- Payments utilising crypto currencies;
- Initial coin offerings;
- Crypto derivatives and funds; and
- Market provisioning.

Refer to Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group *Consultation Paper on Policy Proposals for Crypto* (2019) at 1.3.1. for further information.

[24] The 2019 Consultation Paper is discussed in greater detail in chapter 3 of this Dissertation.

[25] The FATF is an inter-governmental body involved with setting international standards that prevent money laundering and the financing of terrorism. Recommendations for the FATF can be found at: *http://www.fatfgafi.org/publications/fatfrecommendations/documents/regulation-virtual-assets.html.*

[26] D Geral & B Tibane 'South Africa Stepping Up A Gear' *IFLR* 2019, available at: *https://www.iflr.com/article/b1lmxcdn48fnkf/south-africa-stepping-up-a-gear*, accessed on 19 September 2020; See also: South African Reserve Bank National Payment System Department op cit note 14.

[27] The 2020 Position Paper is discussed in greater detail in chapter 3 of this Dissertation.

Crypto Asset Providers (CASP),[28] and how cryptocurrencies may be regulated through CASPs, as well as regulations on cross border transactions and proposed anti-money laundering recommendations.[29]

It must also be noted, that through each published paper, the definition of a 'cryptocurrency' was further developed, and evolved to portray the understanding that these regulatory groups have of cryptocurrencies. The definition of cryptocurrencies will be explained further below.

Hence, it can be observed, that through the SARB, the 2014 Position Paper was published, detailing the underlying nature and risks associated with cryptocurrencies. This position paper was then followed by the 2019 Consultation paper, which was published by the IFWG/CARWG, and provided a development upon the findings of the 2014 Position Paper, focussing on AML/CFT. Lastly the 2020 Position Paper, published by the IFWG/CARWG, used the prior papers as a foundation to develop recommendations as to the manner in which cryptocurrencies may regulated and understood. In addition, it can also be observed that South Africa has moved from classifying cryptocurrency as a 'currency' in the 2014 paper which dealt with *virtual currencies*, to presently, where the IFWG CARWG and SARS classify it as an asset.

It can also be noted that there is a shift in the understanding surrounding the concept of a cryptocurrency. This is evidenced by the change in terminology, which seems to indicate a shift in the thinking of regulatory bodies and is indicative of how cryptocurrencies will be regulated as an asset rather than a currency.

The concept of a crypto asset is introduced in the 2019 Consultation Paper and further developed in the 2020 Position Paper. A crypto asset refers to a collective name used to encompass various crypto-subsets, with one of these forms of crypto-subsets being cryptocurrency. Hence, through these policy papers, the understanding of cryptocurrency has evolved from having a mere understanding of what constitutes a cryptocurrency in terms of technology, to developing a greater understanding that a cryptocurrency falls within a subset known as a crypto asset. This illustrates the evolution in understanding this novel concept. [30]

In addition, it must be understood that these position papers are merely an interpretation of the law by the respective regulatory bodies found within the IFWG and CARWG. These position papers are not

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[28] A CASP refers to:

- Trading platforms that facilitate the purchasing and selling of crypto assets, or the exchange of crypto assets into legal tender, other crypto assets or value of other crypto assets. It's important to note that crypto asset vending machines will be considered as being able to facilitate these activities.
- Digital wallet providers for the storage of crypto assets.
- Crypto asset safe custody.
- Payment service providers who accept crypto assets as a means of exchange.

Refer to Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 23 at 8.8. for further information.

[29] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 23.

[30] The definition of a cryptocurrency and its evolution is discussed in Section II, chapter 2.

the soft-law but are useful in determining how these regulatory bodies perceive the legal framework in relation to use cryptocurrencies within the financial sector of South Africa.

III. TWIN PEAKS MODEL

The FSRA was introduced in 2017, and essentially provides for the existence of the two authorities, namely the PA and FSCA. This Act allowed for the Twin Peaks model to be adopted within the South African financial sector. The main aim of the FSRA is to ensure that the financial system and consumers are safe and secure. In addition, this Act has the aim of ensuring that financial stability is maintained within South Africa.[31]

Through the FSRA, the financial sector was introduced to three changes. These changes focussed on the following:[32]

- Through the FSRA, SARB is given the directive to maintain financial stability of South Africa.
- Within the administration of SARB, a juristic person known as the Prudential Authority (PA) is established.
- A market conduct regulator known as the Financial Sector Conduct Authority (FSCA) is established.

The PA, and FSCA form part of the Twin Peaks model, with each authority representing a 'peak' of the Twin Peaks model.

The PA[33] ensures control over all prudential areas of both banks and other financial institutions that do not operate as a bank.[34]

By contrast to the PA, the FSCA is a regulator that ensures the regulation of markets for those financial institutions that provide both financial services and products. The purpose of the FSCA is to ensure that there is a promotion of fair treatment conducted by financial institutions, therefore allowing for the protection of financial customers. This allows for the FSCA to improve the integrity as well as the efficiency of the general financial market. Promoting financial stability within the financial sector is also a key objective of the FSCA.[35]

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[31] Long title of the FSRA; See also: G Van Niekerk & C Van Heerden 'The Importance of a Legislative Framework for Co-Operation and Collaboration in The Twin Peaks Model of Financial Regulation' (2020) 137 *SALJ* 108 at 115-116.

[32] U Ramracheya 'The Twin Peaks Model – A New approach' op cit note 1

[33] The objectives of the Prudential Authority can be found within S33 of the Financial Sector Regulation Act. In essence however, the Prudential Authority aims to:
'…promote and enhance the safety and soundness of market infrastructures and financial institutions that provide financial products and securities services; protect financial customers against the risk that those financial institutions may fail to meet their obligations; and assist in maintaining financial stability.' U Ramracheya 'The Twin Peaks Model – A New approach' op cit note 1

[34] 'Twin Peaks: Why fix what isn't broken?' (2017) 2017 *Money Marketing* 8 at 1.

[35] 'About Us' *FSCA*, available at: *https://www.fsca.co.za/Pages/Vision-and-Mission.aspx*, accessed on 15 December 2020.

The objectives and aims of both the PA and FSCA can be found within the FSRA, in terms of sections 33(d) and 57(c) of the Act. In order to achieve the aims of the FSRA, the Sections within the Act provides for co-operation to occur between the different financial regulators. For example, to achieve stability within the financial system, the FSRA, through sections 26 and 27, ensure that SARB is able to achieve its general mandate, which is to achieve stability in the financial sector of South Africa. This ensures that the aims of the FSRA are achieved.[36] Hence it can be seen that the FSRA underpins the Twin Peaks Model.

In understanding the aims of the FSRA, it is important to also have an understanding as to how crypto assets impact the regulation in South Africa. As noted in chapter 2 and 3 respectively, crypto assets through their underlying definition and characteristics can circumvent regulations that do not explicitly include the concept of crypto assets within its ambit. In its current state, the FSRA does not include the crypto assets within its ambit. Hence, this could affect the stability of the financial sector and therefore be detrimental to the FSRA.

However, through the 2020 Position Paper,[37] it has been recommended that facilities that provide services relating to crypto assets, be termed a CASP.[38] Furthermore, in relation to CASPs, any services that is conducted and falls within the business of a CASP, must be included within the ambit of the Twin Peaks model. The manner in which crypto assets will therefore fall within the ambit of the Twin peaks model, is that any services performed by CASPs with respect to crypto assets, will be considered as being a 'financial service' in terms of the FSRA.[39] Therefore, it can be noted (with reference to the 2020 Position Paper)[40] that the FSRA will need to be amended in order to include the activities of CASPs within its ambit. Through this amendment, any services offered by a CASP in relation to a crypto asset will be deemed a financial service, therefore allowing for some form of regulation to occur in respect of the FSRA and crypto assets.

In addition to the above, it can also further be noted that the 2020 Position Paper views that the FSCA should oversee the licensing of services in relation to the purchasing and selling of crypto assets. Likewise, the 2020 Position Paper also makes the recommendation that the PA should consider appropriate regulation of crypto assets.[41]

It can therefore be observed that the implication of a CASP being a financial service provider is that all services associated with crypto assets will fall within regulations that is guided by a framework

[36] For further reading, please refer to: G Van Niekerk & C Van Heerden op cit note 31.
[37] Refer to Section I, and Section IV of chapter 3.
[38] Refer chapter 3 Section IV.
[39] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 9; See also: chapter 3, Section IV.
[40] Refer to chapter 3 Section IV.
[41] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 8 and 9.

of legislation. This could provide greater accountability by CASPs as they would have a framework that would allow them to identify suspicious transactions associated with crypto assets and report these transactions.

IV. PRUDENTIAL AUTHORITY

a) *Banks Act 94 of 1990*

The Banks Act is a form of financial regulation that regulates the banking sector, by supervising companies registered in terms of this act, to conduct the business of the bank, through receiving deposits from the general public. A company registered in terms of the Banks Act is seen as a deposit taking institution that can be termed as a 'bank'. Furthermore, the Banks Act prohibits individuals from carrying on the business of a bank, unless the individual has registered a public company, and subsequently has this public company registered as a bank in terms of S11 of the Banks Act.[42] Furthermore, a bank is associated with accepting deposits. In terms of the Banks Act, a deposit is:

> …an equal amount or any part thereof [that] will be conditionally or unconditionally be repaid, either by the person to whom the money has been so paid or by any other person, with or without a premium, on demand or at a specified or unspecified date or in circumstances agreed to by or on behalf of the person making the payment and the person receiving it...[43]

Therefore, it can be understood that a deposit simply refers to money that is given to the bank to keep on behalf of the customer.

Departing from the statutory definition of a bank, the common law understanding of a bank views a bank as being an institution that is concerned with the 'business of banking'. According to the Australian case of *Commissioners of the State Savings Bank of Victoria v Permewan Wright and Co Ltd*,[44] the business of banking is understood to encompass: '…collection of money by receiving deposits on loan, repayable when and as expressly or impliedly agreed upon, and the utilisation of the money so collected by lending it again in such sums as are required.'[45]

Hence, it can be seen that the business of banking encompasses a variety of activities such as deposit, payment and loan activities.[46] As noted by Perlman, the common law understanding of a bank

[42] Banks Act 94 of 1990.
[43] Section 1 of the Banks Act 94 of 1990.
[44] (1914) 19 CLR 457.
[45] L Perlman *Legal and regulatory aspects of Mobile Financial Services* (Phd thesis, University of South Africa, 2012) at 126
[46] Ibid at 124; See also: the business of banking may be determined, as stated by Perlman, Ibid at 126:
'First of all, bank activities can change over time as they take on new business models, becoming multifunctional entities. Secondly, an entity engaged in the 'banking business' in one place is not necessarily considered a bank elsewhere and, thirdly, an entity's reputation may influence the determination.'

should be relied upon to dispel any gaps in understanding the concept of a bank, through the statutory definition.[47] Furthermore, in the case of *United Dominions Trust Ltd v Kirkwood*,[48] the criteria for the business of banking were seen to represent three criteria, namely:

1. The money that has been accepted by the bank, on behalf of customers;
2. the money that is in possession of the bank, is given for payment by the bank, on behalf of customers; and
3. records of such transactions kept on behalf of customers.

Therefore, it can be said that the term 'bank' can refer to an entity who conducts the business of a bank, which includes being a deposit taking institution, that also effects payments and makes a record of such transactions on behalf of their respective consumers. However, although these characteristics can be used to identify the business of a bank, it has been noted by Perlman, that these characteristics may not necessarily result in an entity being a bank. The reason for this is because the reputation of an entity conducting the 'business of a bank' may override the characteristics that may be associated with carrying the business of a bank.[49]

Furthermore, it is also important to understand that banking is based on the concept of 'money'. All deposits, as well as payments must be made with money.[50] Hence, in terms of crypto assets, what is important to understand when determining the applicability of this law, is the concept and definition of 'money'. The Banks Act does not define the term 'money' within the Act itself, but money can be inferred to refer to legal tender. A legal tender can be defined as notes and coins that are issued by a bank and are in circulation within South Africa.[51]

As mentioned in chapter 2, crypto assets – by virtue of their characteristics – are not considered to fall within the definition of legal tender. Therefore, since it does not fall within the meaning of a legal tender, it cannot be categorised as 'money'. Hence, according to the Banks Act, crypto assets are not regulated.[52] However, contrasting the Banks Act, the Value Added Tax Act 89 of 1991 as well as the Tax Law Amendment Bill view a crypto asset as a 'financial service' as opposed to legal tender/money. Furthermore, in terms of the Income Tax Act 58 of 1962, a crypto asset is seen as a 'financial product'.[53]

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[47] L Perlman op cit note 45 at 126.
[48] (1966) 2 QB 431 at 446.
[49] L Perlman op cit note 45 at 129.
[50] Ibid at 129.
[51] Section 17 of the South African Reserve Bank Act 90 of 1989.
[52] Banks Act 94 of 1990.
[53] Draft Taxation Laws Amendment Bill (Draft TLAB) (16 July 2018); See also: 'Cryptocurrency and Tax' *Bowmans* 2019, available at: *https://www.bowmanslaw.com/wp-content/uploads/2018/11/Session-3-Cryptocurrency-and-Tax.pdf*, accessed on 5 November 2020; R Basson 2020, 'An analysis of issues relating to the taxation of cryptocurrencies as financial instruments' (2020) 13 *Journal of Economic and Financial Sciences* 1 at 487.

Furthermore, this perspective is further supported in terms of the 2014 and 2020 Position Paper,[54] as well as the 2019 Consultation Paper[55] which states that legal tender can only be issued by a banking institute and since crypto assets are not considered as legal tender, crypto assets cannot be a substitute of legal tender.[56]

Therefore, it must also be noted that in terms of a CASP, it is important to determine, if such an entity constitutes as conducting 'business of a bank'. As noted in 2019 Consultation Paper, a CASP engages in activities that concern:[57]

- Trading platforms that facilitate the purchasing and selling of crypto assets, or the exchange of crypto assets into legal tender, other crypto assets or value of other crypto assets. It's important to note that crypto asset vending machines will be considered as being able to facilitate these activities.
- Digital wallet providers for the storage of crypto assets.
- Crypto asset safe custody.
- Payment service providers who accept crypto assets as a means of exchange.

Hence, it can be seen that a CASP does not allow for a deposit to occur, whereby money is kept with CASP, in the same sense money would be deposited into bank—as noted in the definition mentioned earlier.[58] The reason this can be said is because when money is deposited to a CASP, it is done so with the intention to purchase crypto assets.

Hence, the CASP, acts as an intermediary to facilitate the exchange, purchase or trade of crypto assets, according to the activities listed above. Furthermore, CASPs merely serve as an exchange, that can convert money, which will be deposited into a crypto asset wallet, into crypto assets and vice versa. It must also be noted that many CASPs offer the service of serving as a crypto asset wallet, and this wallet is merely used to store crypto assets, as well as receive and send crypto assets to other wallets.[59]

Hence, the money that is deposited to a CASP, is not merely kept on behalf of a customer, or used for a payment on behalf of a customer, but is used to be exchanged into a crypto asset, which are then stored by the CASP. Furthermore, a CASP is not seen to have the reputation or alternatively the status of carrying on the business of a bank.[60]

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[54] Refer to chapter 3 for an in-depth analysis of the 2020 Position Paper.
[55] Ibid.
[56] South African Reserve Bank National Payment System Department *Position Paper 02 on Virtual Currencies* (2014).
[57] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 23 at 8.8.
[58] '…an equal amount or any part thereof will be conditionally or unconditionally be repaid, either by the person to whom the money has been so paid or by any other person, with or without a premium, on demand or at a specified or unspecified date or in circumstances agreed to by or on behalf of the person making the payment and the person receiving it...' Section 1 of the Banks Act 94 of 1990.
[59] See: Luno 'Terms of Use' available at: *https://www.luno.com.southafrica.*
[60] F Khoza & Fisser D 'Blockchain Revolution and Financial Regulation in South Africa' *Tech4Law* 2016, available at: *http://www.tech4law.co.za/news-in-brief/59-law/2233*, accessed on: 5 January 2021.

Therefore, it can be noted that crypto assets through CASPs, as well as crypto assets alone do not fall within any definitions of banking and therefore cannot accordingly be regulated in terms of the Banks Act.

b) South African Reserve Bank Act 90 of 1989

The South African Reserve Bank Act (hereinafter referred to as the SARB Act) creates the central bank of South Africa. In addition to creating the central bank of South Africa, this Act provides the mandate for SARB.[61]

The main objective of SARB can be found in section 3 of the SARB Act, which states: 'The primary objective of the Reserve Bank is to protect the value of the currency of the Republic in the interest of balanced and sustainable economic growth in the Republic.'[62]

The SARB Act consolidates all the laws that relate to the South African Reserve Bank (SARB) and the monetary system of South Africa. Through the SARB Act, SARB is considered to be a juristic person that has the primary objective of ensuring that there is protection of the value of the currency of South Africa, and a balance sustainable economic growth. Furthermore, through this Act, the South African Reserve Bank can issue legal tender of South Africa and exercise control over the circulation of money and credit in South Africa.[63]

In essence, SARB controls and manages the legal tender of South Africa. This is further supported in terms of section 14 of the SARB Act, that states that only SARB is allowed to issue legal tender.[64]

However, in terms of SARB, it does not recognise crypto assets as a form of legal tender. The reason for this is that crypto assets fall outside of the definition of legal tender as found within the SARB Act. In terms of section 17 of the SARB Act, it provides that legal tender is a note or coin, for which the Bank has assumed liability in terms of section 15(3)(c) of the Currency and Banking Act.[65]

Hence, in terms of the Act, crypto assets are therefore not found within the scope of the act, and are therefore not regulated in terms of this act.

Furthermore, the perception that crypto assets do not form part of legal tender is further supported by the 2014 Position Paper, which states that: 'DCVCs are not legal tender in RSA and should not be used a payment for the discharge of any obligation in a manner that suggests they are a perfect substitute of legal tender.'[66]

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[61] South African Reserve Bank Act 90 of 1989.
[62] Section 3 of the SARB Act.
[63] South African Reserve Bank Act 90 of 1989.
[64] South African Reserve Bank National Payment System Department op cit note 14 at 3.
[65] Section 17 of the South African Reserve Bank Act 90 of 1989.
[66] South African Reserve Bank National Payment System Department op cit note 14 at 3.2.4.

This position founded in the 2014 Position Paper is further confirmed in both the 2019 Consultation Paper and 2020 Position Paper.[67] Hence, it can be said that the SARB Act does not provide for the regulation of crypto assets, due to the fact that a crypto asset does not fall within the ambit of the meaning of a 'legal tender'.

Therefore, both the SARB Act and Banks Act is not relevant in regulating crypto assets in South Africa. Hence, it can be recommended that SARB should further investigate the nature of crypto assets. Instead of looking at how to regulate crypto assets like legal tender, SARB can look at regulating crypto assets through services associated with crypto assets transactions – much like how the FSRA aims to regulate crypto assets through CASPs.

V. FINANCIAL CONDUCT SECTOR AUTHORITY

a) FICA

FICA established the Financial Intelligence Centre (FIC) and the Money Laundering Advisory Counsel. The aim of FICA, in conjunction with its established bodies is to combat and prevent money laundering as well as other criminal activities, such as the financing of terrorists within South Africa through a risk-based approach.[68]

Through FICA, the Act ensures that South Africa's regulations in relation to money laundering and the prevention of financing terrorists or any other threats to the international financial system are in line with the recommendations and structures present in the intergovernmental body known as the FATF—to which South Africa is a signatory.[69]

FICA provides that all 'accountable institutions' in South Africa must comply with the Act. It is important to understand that an 'accountable institution' in terms of Schedule 1 of FICA, includes a person or organisation who is an attorney, stockbroker, management companies, bankers, foreign exchange brokers estate agents, to name a few. Furthermore, FICA also has an influence on the transactions entered into with clients or consumers who enter into a business relationship with an accountable institution.[70]

FICA assists in identifying transactions (between consumers and accountable institutions) that may be unlawful, involved in money laundering or financing terrorism. Furthermore, FICA also

[67] Refer to chapter 3 for an analysis into all 3 position papers, as well as chapter 2, Section II, Section a for an analysis on the definition of a crypto asset, and the reason it does not constitute as a legal tender; See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 23 at 2.1.1; Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 2.1.1.

[68] C Hugo & W Spruyt 'Money laundering, terrorist financing and financial sanctions: South Africa's response by means of the Financial Intelligence Centre Amendment Act 1 of 2017' (2018) 2 *TSAR* at 227; See also: Financial Intelligence Centre Act 38 of 2001; 'Financial Intelligence Centre Act' *Banking*, available at: *https://www.banking.org.za/consumer-information/consumer-information-legislation/financial-intelligence-centre-act/,* accessed on 25 September 2020.

[69] Ibid.

[70] Schedule 1, Financial Intelligence Centre Act 38 of 2001.

exchanges information with other international bodies with regards to any offences, such as money laundering.[71] In order to identify these transactions, accountable institutions have an obligation under FICA to:

- Identify and verify the identity of clients.[72]
- Keep records of the business relationship between the consumer and accountable institution. [73]
- Report to FIC about consumers, this includes reporting any consumer activities that many contravene the FICA.[74]
- Protection of confidential Information.[75]

Hence, it can be noted that by looking at FICA in its standard state, by virtue of definitions and characteristics, FICA will not apply to crypto asset transactions. The reason for this is because in terms of schedule one, two and three of FICA, CASPs[76] and the actual crypto asset concept is not defined within the schedules, and therefore does not fall within the regulation of the act respectively.

However, although there are no formal regulations for crypto assets, CASPs, such as Luno operate as if they are regulated, by employing 'know-your-customer' (KYC) protocols for crypto asset wallet holders who wish to purchase crypto assets from Luno.[77]

It must be noted that in terms of the 2019 Position Paper,[78] a recommendation was made to include CASPs as an accountable institution, and by virtue of being an 'accountable institution', there will be a legal obligation on the CASPs to comply with FICA.[79] The implication of this suggestion is that it would provide for the administration of CASPs that exchange crypto assets for legal tender and

[71] Financial Intelligence Centre Act 38 of 200.
[72] Section 21 of the Financial Intelligence Centre Act 38 of 2001.
[73] Sections 22—26 of the Financial Intelligence Centre Act 38 of 2001.
[74] In terms of the FICA, accountable institutions will be required to report consumers who enter into either unusual or suspicious transactions, or alternatively engage in unusual and suspicious activities. An example may be if a client attempts to deposit, in cash, an amount of R25000 or greater into an accountable institution's account for a specific payment. However, upon the institution enquiring about the source of the funds from the client, the client refuses to reveal the source and does not proceed to deposit the funds. Therefore, the institution would be required to report the client in terms of a suspicious activity, for not disclosing the source of the funds. Refer to Sections 27—40 of the Financial Intelligence Centre Act 38 of 2001; See also: Financial Intelligence Centre *Guidance Note 4A* (2017).
[75] Section 41 of the Financial Intelligence Centre Act 38 of 2001.
[76] In terms of the South African Reserve Bank Position Paper 2020, CASPs are defined as being a facilitator of crypto asset trading. Hence, this includes services for customers that are:
(i) the purchasing/buying, selling or transfer of crypto assets, including the use of crypto asset vending machine facilities;
(ii) the trading, conversion or exchange of fiat currency or other value into crypto assets;
(iii) the trading, conversion or exchange of crypto assets into fiat currency or other value; and
(iv) the trading, conversion or exchange of crypto assets into other crypto assets.
[77] However, Luno customers that wish to merely store, transfer or receive crypto assets in their respective accounts, do not need to submit to the KYC protocols and can remain anonymous, so long as they do not buy crypto assets using Luno's services. 'Why does Luno Need to Know My Identity' *Luno* 2020, available at: *https://www.luno.com/blog/en/post/%E2%80%8Bwhy-does-luno-need-to-know-my-identity:*, accessed 20 September 2020.
[78] Refer to chapter 3, Section III for an in-depth analysis of the 2019 Position Paper.
[79] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 57.

vice versa, therefore allowing crypto asset transactions to be in line with FICA as well as FATF recommendations in relation to money laundering and funding of terrorism activities.[80]

Furthermore, in terms of the 2020 Position Paper,[81] it's supported that CASPS should be viewed as an accountable institution in terms of FICA, thereby allowing crypto asset transactions to be identified by FICA.[82] Hence, all provisions of FICA will be applicable to CASPs that are registered.[83]

By virtue of being an accountable institution, this would ensure that FIC is the supervisory body over all CASPs. The implication of this is that FIC will be able to enforce compliance as well as penalties against Registered CASPs. In addition to this, by virtue of being registered with FIC, all CASPs will have to ensure that AML/CTF assessments are conducted, and in addition the 'travel rule' is implemented in relation to FATF recommendations.[84]

Furthermore, in June 2020, the Minister of Finance published amendments concerning FICA. One of these amendments included that CASPs be included in terms of schedule one of FICA, thereby making all CASPs in South Africa an accountable institution in terms of FICA.[85]

Hence, it can be seen that through the proposed amendments to FICA, all CASPs will be encompassed in terms of FICA, and therefore all crypto asset transactions made in respect to CASPs will fall under the scrutiny of FIC. This therefore eliminates the previous deficiency of the FICA; whereby crypto assets were not able to be regulated. Therefore, should the amendments to FICA be passed to cater for CASPs being an accountable institution, then FICA would be an appropriate form of regulation in relation to crypto assets.

b) FAIS

The Financial Advisory and Intermediary Services Act (hereinafter referred to as FAIS) deals with the concept of a financial product/service. In terms of the FAIS definition of a financial product, it can be seen as being a security, debenture, participatory interests in one or more collective investment schemes

[80] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Consultation Paper op cit note 57; See also: T Janse van Rensburg 'Proposed amendments to The Financial Intelligence Centre Act, 2001' *Werksman* 2020, available at: *https://www.werksmans.com/legal-updates-and-opinions/proposed-amendments-to-the-financial-intelligence-centre-act-2001/ ,* accessed on 20 September 2020.

[81] Refer to chapter 3, Section IV for an in-depth analysis of the 2020 Position Paper.

[82] Furthermore, CASPs that deal with tokens, as well as alternative/derivative funds would also be required to be considered an accountable institution. Lastly, CASPs that provide custodial services such as a crypto asset wallet will also be considered as an accountable institution. Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 9.

[83] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 8.

[84] Ibid.

[85] S Govender & N Mthembu 'Proposed amendments to FICA schedules' *Bizcommunity* 2020, available at: *https://www.bizcommunity.com/Article/196/717/206072.html*, accessed on 20 September 2020.

or financial instruments. A financial service refers to advice that renders an intermediary service in respect to a financial product.[86]

FAIS ensures that consumers who deal with financial products and services are protected, given adequate information about the financial product/services and are aware of the individuals or organisations that deal with these respective financial products/services. Hence, any individual or organisation who gives a consumer advice about financial products/services is required to be licensed as a Financial Service Provider (FSP) in terms of FAIS. 'Advice' in terms of FAIS is seen as being a recommendation or guidance give to a client or group of clients.[87]

However, FAIS is silent on whether an individual or organisation can give advice on crypto assets. Hence, FAIS does not specify whether crypto assets fall within the tenets of FAIS, and whether an individual or organisation who renders advice about crypto assets to a client, would need to register as a FSP in terms of FAIS.[88]

In November 2020, the FSCA issued a draft Declaration of Crypto Assets, in terms of FAIS. In this Declaration, it highlighted recommendations made in the 2019 Consultation Paper, as well as 2020 Position Paper, and gives effect to these recommendations respectively. This Declaration indicates that crypto assets will be considered as a financial instrument in terms of FAIS. Hence, any individual or organisation that gives advice, trades or sells crypto assets will have to register as a FSP in terms of FAIS. The purpose of this is to ensure that clients who seek advice with regards to crypto assets will be provided with the risks and benefits associated with crypto assets.[89]

In terms of this Declaration, existing CASPs will be seen as FSP, and will need to register for a FSP license in terms of section 8 of FAIS, within four months of the final date of the final Declaration. Until the license is granted, the respective CASPs can still continue to carry on its business. However, should no application for a licence be made, or the application has been declined, then all operations must cease. Furthermore, all new CASPs that begin business after the final date of the final Declaration, will need to apply for a FSP license before the CASPs can commence business.[90]

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[86] Financial Advisory and Intermediary Services Act 37 of 2002; See also: D Reddy, 'FSCA takes first steps in the regulation of crypto assets' *Financial Institutions Legal Snapshot* 2020, available at: *https://www.financialinstitutionslegalsnapshot.com/2020/11/fsca-takes-first-steps-in-the-regulation-of-crypto-assets/*, accessed on 27 November 2020; Financial Sector Conduct Authority, Draft Declaration of Crypto Assets As A Financial Product (2020); 'Financial Advisory And Intermediary Services Act' *The Banking association South Africa* 2020, available at: *https://www.banking.org.za/consumer-information/consumer-information-legislation/financial-advisory-and-intermediary-services-act/*, accessed on 10 October 2020;W Murray, 'The applicability of the Financial Advisory and Intermediary Services Act to cryptocurrency assets' *Cliff Dekker* Hofmeyer 2019, available at: *https://financialregulationjournal.co.za/2019/08/08/the-applicability-of-the-financial-advisory-and-intermediary-services-act-to-cryptocurrency-assets/*, accessed on 10 October 2020.

[87] Ibid.

[88] Ibid.

[89] Ibid.

[90] Ibid.

The implication of the Declaration is that should a CASPs application be successful, then as an FSP, with a FSP license, The CASP will then need to further register as an accountable institution in terms of FICA, and therefore be subjected to relevant AML/CTF regulations to ensure compliance.[91]

Hence, it can be noted that through the Declaration, a concentrated effort is made by FAIS to ensure that risks are mitigated for consumers when dealing with CASPs that offer services to consumers. The Declaration is still open for comment as of writing (final comments close on 28 January 2021). Should this Declaration be passed, it would result in FAIS being a relevant piece of legislation in regulating crypto assets in South Africa.

c) FMA

The FMA's main mandate is to ensure the supervision and regulation of the South African financial market.[92] The financial market can be described as an institutional mechanism that is in existence for the purchasing, or alternatively selling of financial instruments.[93]

Hence, in regulating the financial market, the FMA therefore regulates securities.[94] This is achieved through the regulation of licenses and exchanges, central securities depositories, prevention of insider trading and other market abuses as found within the long title of the FMA.[95]

In therefore understanding the purpose of the FMA, it is important to determine if the FMA is applicable towards crypto assets, specifically in relation to ICO's and security tokens.[96]

As established in chapter 2,[97] The National Treasury was of the view that cryptocurrencies do not fall within the ambit of a 'security' and therefore cannot be regulated in terms of the FMA.[98]

However, that conclusion made by the National Treasury was made in 2014. Since that conclusion was drawn, it has been established by the 2020 Position Paper[99] that the term crypto asset serves as an umbrella term that includes cryptocurrencies as well as exchange or payment tokens; security tokens;

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[91] Ibid.

[92] Long title of the FMA; See also: S Luiz, K Van der Linde 'The Financial Markets Act 19 of 2012: Some Comments on the Regulation of Market Abuse' (2013) 25 *SA Mercantile Law Journal* 4.

[93] H Pakies *The market abuse control legislative regime of South Africa; Nigeria; and the United Kingdom-an approach to regulation and monitoring in relation to certain aspects of financial markets of South Africa* (unpublished LLM thesis, University of Western Cape, 2015) at 4-5; See also: H Chitimira *Overview of the Market Abuse Regulation Under the Financial Markets Act 19 of 2012* North West University 2014.

[94] In terms of Section 1 of the FMA, securities, participation in investment schemes, debentures, units or even listed and unlisted shares

[95] Long title of the FMA.

[96] Refer to chapter 2, Section IV for an in-depth explanation into the various types of crypto assets.

[97] Section II, Section a.

[98] National Treasury, 'User alert: Monitoring of virtual currencies' National *Treasury* 2014, available at: *http://www.treasury.gov.za/comm_media/press/2014/2014091801<percent>20<percent>20User<percent>20Alert<percent>20Virtual<percent>20currencies.pdf,* accessed on 29 June 2020. See also: chapter 1 ss 30–55 of the Financial Market Act 19 of 2012; E Reddy, V Lawack 'An overview of the regulatory developments in South Africa regarding the use of cryptocurrencies '(2019) 31 SA Mercantile Law Journal 1-28.

[99] Refer to chapter 3, Section IV.

utility tokens. In addition to these tokens, ICO's also fall within the scope of a crypto assets.[100] The types of crypto assets that are of importance in relation to the FMA are security tokens and ICO's. The reason for this is because security tokens provide ownership rights, entitlements or a share in profits.[101] On the other hand ICO's provide a manner to increase funds or capital of a business or company using block chain technology. These tokens bear a close resemblance to traditional counterparts that are regulated by the FMA and are recognised as being a security.[102]

In identifying this similarity, it has been recommended by the 2020 Position Paper, that issuers of ICO's/ security tokens should be 'aligned' as close as possible with those of traditional issuers of securities as currently regulated by the FMA. Therefore, through this recommendation, it can be concluded that such crypto assets will fall within the ambit of regulation of the FMA.[103]

Hence, the FMA in its current state do not view a crypto asset as a security, but will need to be amended to include the concepts of an ICO/security token within its ambit, for crypto assets to be regulated, resulting in the FMA being relevant towards crypto asset regulation.

VI. CURRENCY AND EXCHANGES ACT 9 OF 1933

Exchange control in South Africa is regulated by the Exchange Control Act, exchange control regulations as well as Currency and Exchange Manuals. Through the Currency and Exchanges Act, SARB, is able to control the inflow and outflow of capital in the Republic of South Africa. In terms of this Act, it attempts to 'control' capital in the form of money, gold, security, and goods/assets that are to leave the or enter the country from another jurisdiction.[104]

The purpose of this Act is to ensure that financial capital assets in South Africa are preserved and that the movement of these capital assets are controlled, whether it is an inflow or outflow.[105]

In understanding the characteristics of crypto assets, it is a decentralised ledger that is anonymous and does not require a third party to facilitate transactions. In addition, it is not in any considered as a security or legal tender in terms of its understood characteristics,[106] nor does it have a designated asset class, in terms of this Act.[107]

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[100] Refer to chapter 2, Section III for an in-depth analysis of the types of crypto assets.
[101] J Frankenfield 'Initial Coin Offering' *Investopedia* 2019, available at: *https://www.investopedia.com/terms/i/initial-coin-offering-ico.asp*, accessed on: 1 June 2020.
[102] K Kopke 'How do you classify cryptocurrency as an investment?' (2018) 18 *Without Prejudice* 2; See also: K Mitchell 'Blockchain IPOs: Capital Raising in the Crypto-World' (2019) 19 *Without Prejudice* 1.
[103] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 9.3.2.1, Recommendation 22.
[104] Currency & Exchanges Act 9 of 1933.
[105] Ibid.
[106] South African Reserve Bank National Payment System Department op cit note 14.
[107] Currency & Exchanges Act 9 of 1933.

Hence, for the application of this Act, it must be emphasised that it applies to the regulation of cross-border movement of capital. However, crypto assets clearly do not fall within the categories of what is considered 'capital' in terms of the Currency and Exchanges Act.[108]

Furthermore, it must be noted, that in order to further enforce currency and exchanges regulations, SARB utilises the services of the Financial Surveillance Department of the Bank (FinSurv).[109] Hence, all cross-border transactions require prior approval from FinSurv. Furthermore, authorised dealers must report cross-border transactions to FinSurv for approval.[110]

In terms of the Currency and Exchanges Manual for Authorised Dealers, it is noted that each South African resident has a Foreign Capital Allowance of ten million Rand to transfer offshore for investment purposes and a Single Discretionary Allowance (SDA) of one million Rand to transfer offshore for the purposes of investments, or gifts. Both of these discretionary limits are applicable for a single calendar year. The Foreign Capital Allowance and SDA essentially serve as being a threshold for South Africans residents in respect to offshore investments. [111]

The reason this is important to understand is because in terms of the 2014 Position Paper, SARB acknowledged there is no regulation in relation to crypto assets, hence if a person intended to purchase crypto assets offshore, then the only recognised manner of purchasing crypto assets is through the use of these discretionary limits in terms of legal tender. However, the value of a crypto asset in a wallet does not form part of the discretionary limits, hence a transfer of crypto assets from a South African wallet to an offshore wallet is not permissible in terms of the discretionary limits. These discretionary limits are only applicable to individuals and not co-operations or organisations, who use legal tender. Hence should this method be relied upon; it can be said that the purchasing of offshore crypto assets from South Africa with legal tender will require authorised dealers to report such transactions to Finsurv.[112]

However, when transactions/transfers that involve crypto assets solely, are facilitated, Exchange Control Regulations still need to be abided by. As noted by Gerald and Tibane, the transfer of crypto

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[108] Capital can be inferred to represent money or legal tender, gold or securities as found within the Currency & Exchanges Act 9 of 1933.

[109] 'In terms of the Regulations, South African residents are afforded a foreign capital allowance of four million Rand per calendar year. These funds may be transferred abroad and invested in any manner without prior approval from the Financial Surveillance Department of the Bank (FinSurv)', South African Reserve Bank National Payment System Department op cit note 14 at 4.3.5.2, 2014.

[110] 'An Authorised Dealer is a person authorised by the Financial Surveillance Department to deal in gold or to deal in foreign exchange, for transactions relating to gold and foreign exchange respectively.' 'Authorised Dealer' *South African Reserve Bank*, available at: *https://www.resbank.co.za/en/home/what-we-do/financial-surveillance/authorised-dealers*, accessed on 14 September 2020.

[111] D Geral & B Tibane 'South Africa Stepping Up Gear' op cit note 26; See also: South African Reserve Bank National Payment System op cit note 14.

[112] Ibid.

assets from a wallet held in South Africa to an offshore wallet *may* be regarded as an *export of capital* in terms of regulation 10(1)(c) of the Exchange Control Regulations of 1961.[113]

Hence, as further noted by Gerald and Tibane, such a transaction will need exchange control approval from FinSurv. The practical challenge and issue at hand is that SARB presently, does not permit FinSurv and authorised dealers to approve these types of transactions involving crypto assets, due to the characteristic and nature of crypto assets.[114]

Hence, the transfer of crypto assets in and out of South Africa are not supported by regulations. Although there are Exchange Control Regulations to facilitate this type of transaction, SARB is yet to support and recognise crypto asset transactions. This may result in the flow of crypto assets that circumvent exchange control regulations of South Africa, as FinSurv will not be able to report or be notified about and 'exports of capital' in the form of crypto asset transfers.[115]

In noting the above, the 2020 Position Paper,[116] made recommendations to ensure a more cohesive exchange control regulation is created in relation to crypto assets.

As it stands presently, crypto assets do not fall within the definition of capital. Hence, it is proposed by the 2020 Position Paper that Exchange Control Regulation 10(4) should be amended to include crypto assets within the scope of 'capital'. Should this proposal be achieved, then this would allow Exchange Control Regulations 10(1)(C) to be applicable to crypto assets.[117]

In addition, it has also been proposed, that FinSurv should recognise and occupy a supervisory/regulatory role in relation to crypto assets. The implication of this proposal is that through FinSurv, SARB will therefore then recognise crypto assets, and permit FinSurv to report cross-border crypto asset transactions. Hence, this recommendation would allow the complete functioning of Exchange Control Regulations, in conjunction with FinSurv. [118]

In addition, it is also proposed that authorised dealers have to capability to facilitate these crypto asset transactions. Furthermore, it is proposed that a crypto asset trading place be identified as an Authorised Dealer in exchange with limited authority. This would therefore also lead to allowing CASPs to therefore facilitate offshore transactions in relation to crypto assets as well as give the responsibility to CASPs to report to FinSurv on cross-border transactions.[119]

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[113] In terms of Regulation 10(1)(c), it does not allow an individual to directly or indirectly export capital out of South Africa, without the permission of SARB. This also applies to the sale and purchase of crypto assets. D Geral & B Tibane 'South Africa Stepping Up Gear' op cit note 26.
[114] Ibid.
[115] South African Reserve Bank National Payment System Department op cit note 14 at 4.3.5.4.
[116] Refer to chapter 3, Section IV.
[117] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper op cit note 17 at 9.1.2.4., Recommendation 12; Refer to chapter 3, Section IV.
[118] Ibid at 9.1.2.3., Recommendation 11; Refer to chapter 3, Section IV.
[119] Ibid at 9; Refer to chapter 3, Section IV.

In noting the above, it can however be observed that SARB is taking a proactive approach in modernising its views with regards to Exchange Control Regulation. This can be supported by exchange controls relating to South African owned intellectual property.

Previously, if a South African company transferred its intellectual property to an offshore company, then there would be a need for approval of transfer/license of the trademark from the exchange control authorities, in terms of the Currency and Exchange Act or SARB, depending on the nature of the transaction. This process was often complicated, and deterred foreign investors.[120]

Hence, in 2020, through the National Treasury's Budget Review, it was indicated that there would be no approval required for the transfer of intellectual property.[121]

Consequently, it can be seen that SARB has the intention to modernise itself as well as have an appreciation for the global economy.[122]

Therefore, through this statement, it can be inferred that there is a probability that SARB in the future would consider the 2020 Position Paper proposals in order to shape exchange control regulations to include crypto assets within its purview.

In addition, it can be noted that through the 2020 Position Paper proposals, it would allow Exchange Control Regulations to be viable in monitoring cross-border transactions involving crypto assets.

VII. CONCLUSION

It can be noted that through research, the relevant Acts concerned with the FSCA can be relevant in regulating the market conduct in relation to crypto assets if amendments are made in line with the proposals highlighted in terms of the 2019 Consultation paper and 2020 Position Paper.

However, in terms of the Banks Act and SARB Act, due to the fact that crypto assets do not fall within their respective definitions of a 'bank' or legal tender, the regulations associated with these Acts

[120] Through commercialisation, trademarks are often traded as an intangible asset/property between businesses. When this occurs between business that are incorporated in the Republic of South Africa i.e., local businesses, the transfer is often uncomplicated and straightforward. However, should a transfer or licensing of trademark be dealt with a company that is South African and an offshore/international company, then complications occur due to the exchange control regulations, which require either SARB or authorised dealers to approve the transfer. Should no approval be granted from the exchange control authorities, then the transfer/license of the trademark is unlawful and unenforceable. O Dean, 'Keep the Trade Mark Assignment Baby When Throwing Out the Bathwater' *Sun* 2021 available at: *http://blogs.sun.ac.za/iplaw/files/2012/08/Keep-the-Trade-Mark-Assignment-Baby-When-Throwing-Out-the Bathwater.pdf,* accessed on 3 October 2020; See also: O Dean & A Dyer *Introduction to Intellectual Property Law* (2014) ch 9; A Visser & A Jefferys 'South Africa: Proposed Changes To South African Exchange Controls Regulating To The Transfer And License Of SA-Owned Intellectual Property' *Mondaq* 2020, available at: *https://www.mondaq.com/southafrica/export-controls-trade-investment-sanctions/938402/proposed-changes-to-south-african-exchange-controls-relating-to-the-transfer-and-license-of-sa-owned-intellectual-property*, accessed on: 19 January 2021.

[121] Ibid.

[122] Ibid.

do not then encompass crypto assets. This results in the respective Acts not being relevant in the regulation of crypto assets.

In terms of Exchange Control Regulations, as highlighted above, relevant changes need to be affected in order to ensure that SARB, through FinSurv recognise crypto assets, therefore allowing existing exchange control regulations to function and regulate cross border crypto asset transactions.

In conclusion, it can be observed that the impact crypto assets have on regulations is that it requires regulatory bodies to ensure that there is greater emphasis made to interpret crypto assets in relation to existing laws, so that existing laws can be amended to include crypto assets, and therefore the subset cryptocurrency within the relevant legislations regulation.[123]

However, it must be noted, that as the law stands as of writing this dissertation, these amendments have not been made. Hence, this results in existing regulatory bodies and regulations not having any authority over crypto assets.

[123] The legislation must form a cohesive network to encompass crypto assets, rather than pieces of legislation that are either contradictory (such as SARB's stance on crypto assets, preventing the operation of regulation 10(1)(c) of the exchange control regulations) or act in isolation in regulating crypto assets. South Africa is on a positive path, with proposed amendments and declarations made in respect to FAIS and FICA. This shows that regulators aim to carefully make legislation to regulate crypto assets in South Africa and protect users of crypto assets and the financial sector as a whole.

CHAPTER 5
A COMPARATIVE ANALYSIS OF THE INTERNATIONAL REGULATION OF CRYPTO ASSETS

I. CHAPTER OVERVIEW

This chapter is going to provide an analysis into the existing cryptocurrency regulations found within the jurisdictions of the United Kingdom (UK) and the United States of America (USA). The aim of this chapter is to analyse the two jurisdictions with a view to suggest recommendations for cryptocurrency regulations, within South Africa. The term crypto asset will be used in relation to the UK and USA where applicable.[1]

It must be noted that around the world, a single harmonised approach to regulate cryptocurrency, and its resultant class, crypto assets is not present. Instead, each country has either adopted regulations or alternatively have completely banned the use and trade of cryptocurrency.[2]

Hence, it is important to analyse countries such as the UK and USA, who have taken the initiative to make innovative regulations aimed at regulating the flow of cryptocurrency in and out of their respective economies. According to Chohan, USA is seen as a leader for setting precedent in relation to the regulation of cryptocurrency through its regulatory bodies known as the Securities and Exchange Commission (SEC) as well as the Commodities and Futures Trading Commission. (CFTC).[3]

In addition, it can be observed that the UK has a similar stance as South Africa, towards the regulation of cryptocurrencies, and this is worthy to analyse against South Africa's existing regulations and stance.

Therefore, through this chapter, the approaches utilised by these respective jurisdictions can be compared to that of South Arica, to determine if existing regulations in South Africa can adopt certain the approaches used in foreign jurisdictions.

In terms of crypto assets,[4] the Financial Conduct Authority (FCA),[5] an authority found within the UK is the primary regulatory body of crypto assets in the UK. Furthermore, the UK established the

[1] Crypto asset includes the subclass cryptocurrency.

[2] Countries such as Bolivia and Ecuador view crypto assets such as Bitcoin being illegal within their jurisdictions. Contrasting the illegality found in these countries, countries in the Middle East, such as Saudi-Arabia, Lebanon and Jordan have not banned the use of crypto assets, but have adopted a stance that discourages the use of crypto assets. W Chohan, 'Assessing the Differences in Bitcoin & Other Cryptocurrency Legality Across National Jurisdictions' 2017 *SSRN Electronic Journal*.

[3] Ibid.

[4] Within the UK, legislators refer to crypto assets as a single word, being 'cryptoassets'. For the purposes of this paper, and the understanding developed in South Africa, the term 'crypto asset' will be utilised.

[5] The FCA is a conduct regulator that regulates areas of financial law. Through this authority, the promotion of fair competition to benefits consumers, protection of consumers and ensuring market integrity is the core goals of the FCA. This regulatory body operates independently of the UK government.

'Cryptoasset Taskforce' in 2018 to assess the developing interest in crypto assets, and provide an understanding in determining the impacts and risks that could be associated with crypto assets.[6]

The stance the UK has in relation to crypto assets can mainly be found within the 'Cryptoasset' Taskforce's Final Report (hereinafter referred to as the 2018 Report). This report, provided an overview on the topic of crypto assets and also analysed the proposed risks and benefits associated with the use of crypto assets. The 2018 Report merely highlights the regulatory approach that can be adopted by regulatory bodies in the UK to regulate the use of crypto assets. Hence, this report is not law but merely provides informative knowledge and recommendations as to how crypto assets may be regulated.[7] Following the 2018 Report, the FCA released various policy statements in 2019, 2020 and 2021. These policy statements built upon the knowledge established in the 2018 Report.

Therefore, it can be noted that, like South Africa, the UK has built a comprehensive understanding of crypto assets through various regulatory bodies engaging in analysing this technology and proposing prospective manners in which crypto assets can be better understood and regulated within the UK.

Contrasting the UK, the USA has crypto asset regulation at both a federal and state level. At a state level it must be noted that there are various proposals and regulations that are followed in relation to crypto assets by each respective State. However, for the purposes of this discussion, regulations at Federal level will be discussed. At a Federal level, the following bodies provide regulation and a greater understanding for when crypto assets are being dealt with:

- Securities and Exchange Commission (SEC)
- Commodities and Futures Trading Commission (CFTC)
- Internal Revenue Service (IRS)
- Financial Crimes Enforcement Network (FinCEN)

In addition to these regulatory bodies, there are various legislative acts that are applied at a federal level to ensure that crypto assets are regulated within the USA. For the purposes of this dissertation, the SEC, CFTC, and FinCEN will be given particular focus.[8]

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[6] The 'Cryptoasset Taskforce' consisted of the following parties:
- Senior representatives from the Bank of England
- FCA
- HM Treasury
- Payment Systems Regulator

[7] Cryptoasset Taskforce *Final Report* (2018).

[8] The IRS oversees the collection of tax in the USA. In terms of the IRS, it recognises that crypto assets are not a form of legal tender, but is merely a form of property. J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' *Global Legal Insights* 2020, available at: *https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/usa*, accessed on 25 October 2020; See also: L Sadhaseevan, *The Regulation of Cryptocurrency in the Context of the South African Financial Sector*, Masters of Business law, UKZN 2019.

II. UNITED KINGDOM

a) Definition

The Report utilises the term 'crypto asset' and refers to it as a broad category. It is understood that traditional cryptocurrencies such as Bitcoin, as well as crypto asset tokens, which are issued for the purpose of being an ICO, are found within the ambit of 'crypto assets'. According to the report, a crypto asset refers to a: 'cryptographically secured digital representation of value or contractual rights that uses some type of DLT and can be transferred, stored or traded electronically.'[9]

Consequently, the FCA published a policy statement, titled the 'Guidance on Cryptoassets', which further clarified and developed the UK understanding of what constitutes as a crypto asset. It was found that in addition to the definition of crypto assets (as determined in the Report), crypto assets also encompass three categories known as e-money tokens,[10] security tokens[11] and unregulated tokens.[12]

In addition, the policy statement provided an explanation for Stablecoins, and how Stablecoins are understood to be regulated. The policy statement attempted to categorise Stablecoins within the ambit of unregulated exchange tokens, or e-money tokens.[13]

Furthermore, in terms of the UK Jurisdiction Taskforce, which released a report in 2019, found that crypto assets are regarded as a form of property in the UK, that can also serve as a form of security. However, due to its nature of not being able to be physically possessed as a security, a crypto asset cannot serve as a lien or pledge.[14]

The definition of a crypto asset was further clarified in the 2021 HM Treasury consultation paper, which merely confirmed the findings of previous policy statements and reports released by various regulatory bodies in the UK unto January 2021.[15]

In addition to these regulatory bodies, the HM Revenue and Customs (HMRC) – the tax authority of the UK, has confirmed the definition and findings of the Taskforce in their various policy papers. Within these policy papers it was emphasised that crypto assets refer to financial technology that is

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[9] Cryptoasset Taskforce op cit note 7 at 2.10; See also: S Davis, S Maxson & A Moyle 'Blockchain & Cryptocurrency Regulation 2021' *Global Legal Insights* 2021, available at: *https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/united-kingdom*, accessed on 12 January 2021.

[10] As noted by the HM Treasury, e-money tokens refer to: '…broadly, digital payment instruments that store value, can be redeemed at par value, at any time and offer holders a direct claim on the issuer', HM Treasury *UK regulatory approach to cryptoassets and stablecoins: Consultation and call for evidence* 2021 at 1.12.

[11] Security tokens refer to crypto assets that have a similar characteristic to investments, like a share or debt instrument. Ibid.

[12] These refer to tokens that either exchange tokens, for example Bitcoin, or alternatively are utility tokens that are used for example, for the purchasing of services. Ibid.

[13] Ibid at 1.15; See also: Financial Conduct Authority *Guidance on Cryptoasset* PS19/22. for further discussion on Stablecoins, refer to chapter 2, Section II and chapter 3, Section IV.

[14] UK Jurisdiction Taskforce *Legal Statement on Cryptoassets and Smart Contracts*; See also: D Murray & N Petrie 'UK: A Mix Of Clarity And Confusion: Crypto Asset Law And Regulation In The UK' *Mondaq* 2020, available at: *https://www.mondaq.com/uk/fin-tech/986964/a-mix-of-clarity-and-confusion-crypto-asset-law-and-regulation-in-the-uk*, accessed on 10 January 2021.

[15] HM Treasury op cit note 10.

'cryptographically secured digital representations of value or contractual rights'.[16] Through this understanding, crypto assets can then be transferred, stored or even traded between relevant parties. Furthermore, the policy papers have confirmed the categories of crypto assets, as stated by the 2018 Report.

However, in light of these findings, it is imperative to understand that the UK does not consider crypto assets to be legal tender.[17]

b) Regulation

The UK, much like South Africa, does not prohibit the use of crypto assets, nor does it have a defined regulatory framework to ensure the regulation of the use of crypto assets within its borders. This is due to the fact that crypto assets are not considered as legal tender. The resultant implication of not being considered a legal tender is that financial regulations that pre-date the creation of crypto assets, will not be able to regulate crypto assets, as crypto assets do not fall within the ambit of the legislation. This further impacts the legal action that can be taken in relation to crypto assets as many existing legislations do not allow for the regulation of crypto assets by virtue of a crypto asset not being considered a legal tender.[18]

However, as mentioned above, the FCA is the primary regulator for crypto assets within the UK. The FCA has refined the definitions and categorisation of crypto assets as found in the 2018 Report. The FCA views crypto assets as being either regulated or unregulated. This distinction is drawn based on the category of crypto asset being dealt with. Hence, if a crypto asset is regulated, then the crypto asset will fall within two categories, namely being a security token or e-money token. However, should a crypto asset be considered as being unregulated, then it would be considered as an unregulated token.[19]

Regulated crypto assets are seen as being subjected to financial regulation. Hence, e-money tokens, are regulated in terms of the Electronic Money Regulations 2011, as the e-money tokens fall within the ambit of the definition of e-money in the regulations.[20] Furthermore, in terms of security

[16] HM Revenue and Customs *Cryptoassets: Tax for Individual.*
[17] S Davis, S Maxson & A Moyle 'Blockchain & Cryptocurrency Regulation 2021'op cit note 9.
[18] Ibid.
[19] Ibid; See also: 'Cryptoassets: Our work' *Financial Conduct Authority* 2019, available at: *https://www.fca.org.uk/firms/cryptoassets*, accessed on 12 January 2021.
[20] E-money tokens, according to the Electronic Money Regulations 2011, are seen to be 'digital payment instruments that store value, can be redeemed at par value, at any time and offer holders a direct claim on the issuer'. HM Treasury op cit note 10 at 1.12.

tokens, these tokens will fall within the ambit of the Money Laundering, and Terrorist Financing and Transfer of Funds Regulations 2017 (FSMA),[21] and are therefore regulated as being a security.[22]

However, although security tokens as well as e-money tokens may be subjected to 'regulations' based on the above explanation, it must be noted that the FCA highlights that any crypto asset investments will be done at the risk of the consumer, and that there cannot be a reliance on any form of consumer protections that may be available for traditional forms of investments.[23]

In terms of unregulated crypto assets, this category consists of utility tokens and exchange tokens.[24] Exchange tokens are what traditional crypto assets are categorised under, as this category is associated with being decentralised and encompassing traditional crypto assets such as Bitcoin and Ethereum. Therefore, any transactions involving exchange tokens is seen as being an unregulated transaction.[25]

In terms of Stablecoins,[26] it has further been established that the manner in which its underlying value is collateralised will determine whether a Stablecoin is either considered to be an unregulated or regulated crypto asset.[27]

Furthermore, the UK has proposed further regulation to ensure AML requirements are met. This is achieved through the requirements found within the Money Laundering, and Terrorist Financing and Transfer of Funds Regulations 2017 (MLR). All AML/CTF requirements are supervised by the FCA.[28]

Through the MLR, the fourth European Union (EU) money laundering directive is utilised,[29] to impose requirements on businesses that can be identified as having the potential to engage in the financing of terrorism or money laundering. Through this directive, the MLR provides for various

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[21] A security token refers to a form of crypto asset that has a nature that is the same or similar to that of a traditional investment like a share or debt instruments as envisaged within UK legislation. Security tokens tend to include digital forms of investments that are already regulated in terms of the FCA. Ibid.

[22] S Davis, S Maxson & A Moyle 'Blockchain & Cryptocurrency Regulation op cit note 9; See also: 'Cryptoassets: Our work' *Financial Conduct Authority* op cit note 19.

[23] Traditional protections come in the form of the Financial Ombudsman Service (FOS) or the Financial Services Compensation Scheme (FSCS). 'Cryptoassets: AML/CTF regime' *Financial Conduct Authority* 2021, available at: *https://www.fca.org.uk/firms/financial-crime/cryptoassets-aml-ctf-regime,* accessed on 12 January 2021; See also: Financial Conduct Authority op cit note 13; 'FCA warns consumers of the risks of investments advertising high returns based on cryptoassets' Financial Conduct Authority 2021, available at: *https://www.fca.org.uk/news/news-stories/fca-warns-consumers-risks-investments-advertising-high-returns-based-cryptoassets,* accessed on 12 January 2021; R Browne 'Cryptocurrency investors should be prepared to lose all their money, Bank of England governor says' *CNBC* 2021, available at: *https://www.cnbc.com/2021/05/07/bank-of-englands-bailey-crypto-investors-risk-losing-all-their-money.html*, accessed on 18 may 2021.

[24] Unregulated crypto assets (as referred to by the FCA) also refer to exchange tokens as found in the Report, and the terms can be used interchangeably; See also: Unregulated tokens consists of utility and exchange tokens. Utility tokens refer to any form of crypto asset used to purchase a service such as cloud storage, whilst an exchange token refers to crypto assets like bitcoin. HM Treasury op cit note 10 at 1.12.

[25] Financial Conduct Authority op cit note 13.

[26] Refer to chapter 2, Section II, Sub-Section a; and chapter 3 Section IV, for an explanation on Stablecoins.

[27] S Davis, S Maxson & A Moyle 'Blockchain & Cryptocurrency Regulation 2021'op cit note 9.

[28] Ibid.

[29] The fourth EU directive on money laundering is available at: *https://eur-lex.europa.eu/legalcontent/EN/TXT/HTML/?uri=CELEX:32015L0849&from=EN* .

mechanisms to ensure that money laundering and funding of terrorism does not occur. Such mechanisms may include record keeping of relevant information pertaining to the business, customer due diligence, or the presence of risk assessment protocols.[30]

However, in 2020, the MLR was amended, to include the recommendations made by the FATF regarding AML requirements and the fifth EU directive in terms of money laundering and funding of terrorism. Through this amendment, MLR would now be able to also regulate all Crypto Asset Providers as well as Custodian Wallet Providers. In terms of the Part 2, Section 14A of the amended MLR, a Crypto Asset Provider refers to any business that conducts the services of either exchanging, crypto assets for other forms of crypto assets, exchanging crypto assets for legal tender and vice versa, or operating a crypto asset ATM for facilitating an exchange.[31]

Contrasting a Crypto Asset Provider, a Crypto Wallet Provider refers to a business that is involved in the services of storing crypto assets or cryptographic keys on behalf of customers.[32]

Furthermore, the MLR requires businesses that fall within the definition of Crypto Asset Provider or Crypto Wallet Provider to register with the FCA in order to implement relevant AML/CTF requirements as found within MLR. Should such businesses not register with the FCA by 10 January 2021, then these businesses would have to cease all forms of trading. However, should businesses trade without complying with the MLR, a criminal offence will be committed.[33]

As it can be noted, the UK has a similar approach to the regulation of crypto assets as South Africa. Various policy papers were released just as South Africa did in order to further develop the understanding and manner in which crypto assets could be regulated. However, the key features that can be noted in terms of the UK, is that firstly crypto assets are not defined as a legal tender. This results in a crypto asset as either being regulated or unregulated depending on its categorisation. Should a crypto asset be considered as a form of e-money or a security, in terms of a security token, crypto assets will then be regulated. This is a key perspective that can be adopted by South Africa in regulating crypto assets. Currently South Africa does not view a crypto asset as being e-money, or a security. It must however be noted that the 2020 Position Paper has recommended that a crypto asset fall within the definition of a security in terms of the FMA.[34]

Should crypto assets be considered as e-money/security, then this would allow for a greater amount of legislation to apply within South Africa, in the regulation of crypto assets.

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[30] S Davis, S Maxson & A Moyle 'Blockchain & Cryptocurrency Regulation 2021'op cit note 9 ; For further understanding please refer to: 'Cryptoassets: AML / CTF regime' op cit note 23; 'FCA establishes Temporary Registration Regime for cryptoasset businesses' *Financial Conduct Authority* 2020, available at: *https://www.fca.org.uk/news/press-releases/fca-establishes-temporary-registration-regime-cryptoasset-businesses,* accessed on 12 January 2021.
[31] Ibid.
[32] Ibid.
[33] Ibid.
[34] Refer to chapter 3, Section IV, Sub-Section c.

It can also be noted, that in terms of consumer protection laws, South Africa fares similarly to the UK, whereby the Consumer Protection Act 68 of 2008 is relied upon by consumers who utilises the services of CASPs within South Africa. In the UK, consumer protections laws will only apply to the transaction that would occur between a consumer and a CASP.[35]

As of 6 January 2021, the FCA has also further banned the trade of crypto asset derivatives by firms offering investments in crypto assets.[36] The implication of this banning is that the FCA aims to protect consumers who may be vulnerable to the price volatility associated with crypto-derivatives. In addition, the FCA has warned consumers of the risks in investing in firms offering crypto asset investments, stating that that such investments, due to the crypto asset nature, may not be offered the full protection offered by the financial industry.[37]

Contrasting the FCA, it can be noted that in 2021, South Africa's market regulator, the FSCA also released their own warning in relation to crypto asset investments, emphasising that investors are of the inherent risk and that there is no legal recourse for experiencing losses in crypto asset investments as the FSCA as well as other regulatory bodies in South Africa, does not currently regulated crypto assets.[38] Through these warnings, it further emphasises the similarities that is present between South Africa and the UK.[39]

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[35] In terms of Consumer Protection Legislation, it can be noted that through the sale of crypto assets as well as those businesses that provide crypto asset services, crypto assets can be regulated in terms of existing consumer protections, as found within the Consumer Rights Act 2015 and the Consumer Protection from Unfair Trading Act 2008. However, it must be emphasised, that these laws do not explicitly regulate crypto assets, but regulate the transaction or service that occurs between a business and its respective consumer. S Davis, S Maxson & A Moyle 'Blockchain & Cryptocurrency Regulation 2021'op cit note 9; See also: 'The Regulatory Status Quo of Cryptocurrency Exchanges' *Go Legal* 2019, available at: *https://www.golegal.co.za/cryptocurrency-exchanges-regulatory/*, accessed on 10 December 2020.

[36] A derivative traditionally refers to an agreement between two or more parties based on the future potential price of an asset of which the agreement is based on. This is normally done to either speculate on the price of an asset or hedge risk on the price of an underlying asset, should the price change. The derivative market refers to commodities such as futures, options and derivative contracts. Derivatives are therefore found in crypto assets, and allow individuals to hedge their risk against crypto assets, allowing a mitigation of risk. For more information please see: *https://cointelegraph.com/explained/derivatives-in-crypto-explained*. See also: 'FCA Bans the Sale of Crypto-derivatives to Retail Consumers' *Financial Conduct Authority* 2020, available at: *https://www.fca.org.uk/news/press-releases/fca-bans-sale-crypto-derivatives-retail-consumers*, accessed on 10 January 2021.

[37] 'FCA warns consumers of the risks of investments advertising high returns based on cryptoassets' *Financial Conduct Authority* 2021, available at: *https://www.fca.org.uk/news/news-stories/fca-warns-consumers-risks-investments-advertising-high-returns-based-cryptoassets*, accessed on 12 January 2021.

[38] The FSCA crypto asset warning can be found at: *https://www.fsca.co.za/News%20Documents/FSCA%20Press%20Release%20%20Crypto%20health%20warning%2004%20February%202021.pdf*, accessed on 5 February 2021.

[39] It must however be noted that through Brexit, the UK may be given more freedom to evolve its financial laws in line with fintech, due to the fact that it will not be part of the European Union, and will not have to follow the European Union's mandates in relation to financial regulation. The manner in which British regulation in relation to crypto assets will evolve post Brexit is a topic to observe. Please see: https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/after-brexit-freedom-to-set-own-rules-in-fintech-crypto-could-benefit-uk-62016052, for further reading.

III. UNITED STATES OF AMERICA

The USA has developed legislation for the effective regulation of cryptocurrencies within their country. Compared to the UK as well as South Africa, it can be observed that the USA has a far more robust form of regulation in relation to cryptocurrencies. The USA has both State and Federal level regulations in relation to cryptocurrencies.[40] However, in the UK as well as South Africa, regulation occurs at simply one level, namely through the legislation applicable to the entire country, the equivalent of the USA Federal regulations. For the purposes of this dissertation, a focus will be kept solely at a Federal level.[41]

In analysing the Federal level, the regulatory bodies can be observed to provide direction as to how cryptocurrency can be regulated. Furthermore, it must be noted that the USA does not utilise a collective term of 'crypto asset' like the UK or South Africa, and instead simply utilises the term 'cryptocurrency'. The term cryptocurrency will therefore be utilised in this part of the discussion.

a) Definition

In terms of Federal laws, there is no specific definition of a cryptocurrency[42] that is developed by Federal regulators. Instead, a general technological understanding forms the basis of the perspective employed by Federal regulators in relation of what constitutes a cryptocurrency.[43]

However, in addition to the technological understanding utilised by Federal regulators, leading cases such as *United States v Ulbricht,*[44] and *SEC v Trendon T. Shavers and Bitcoin Savings and Trust Case*[45] have helped to provide a greater understanding as to how cryptocurrencies may be defined.

[40] There have been various approaches adopted by various States in regulating crypto assets. Some States have introduced laws to ensure the promotion of crypto assets whilst other states have introduced laws that stifle the promotion of crypto assets. However, where a State law is in conflict with Federal law, Article IV, Clause 2 of the Supremacy Clause contained in the United States Constitution will be relied on, as it allows for Federal law to take precedence over State law in the event of a conflict between these laws. For further information please refer to: J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8; See also: A Hamilton 'Digital states: Cryptocurrency rules and regulations across the US' *Bobs Guide* 2019, available at: *https://www.bobsguide.com/guide/news/2019/Feb/8/digital-states-cryptocurrency-rules-and-regulations-across-the-us/*, accessed on 10 January 2021.

[41] In addition to Federal law, it must be highlighted that that at a State level, each State has their own rules and legislations in regulating cryptocurrency transactions. There is no uniformity between the States. For further reading on State regulations, please refer to; M Koehn & J Wales ' State Regulations on Virtual Currency and Blockchain Technologies' *Carlton Fields* 2020, available at: *https://www.carltonfields.com/insights/publications/2020/state-regulations-on-virtual-currency-and-blockchain-technologies-(updated-july-2020),* accessed on: 19 January 2021.

[42] Cryptocurrency may be referred to as a digital asset, crypto, virtual currency or even digital tokens; See Also: J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8.

[43] Refer to chapter 2 for an in-depth analysis relating to the underlying technology and understandings that underpin the concept of a crypto asset.

[44] No. 15-1815 (2d Cir. 2017).

[45] No. 4: 13-CV- 416 United States District Court.

In the case of *United States v Ulbricht,*[46] the Court analysed the general meaning of Bitcoin, and it was understood that cryptocurrency does not fall within the classification of a legal tender, but as an intangible asset that has value.[47]

Furthermore, in the case of *SEC v Trendon T. Shavers and Bitcoin Savings and Trust*[48] stated that since cryptocurrencies have the potential to be used to purchase goods and services and furthermore be exchanged for conventional legal tender, as well as be seen as a form of money and therefore can be inferred to be an investment of money.[49] Hence, from these cases it can be seen that, in addition to general technological characteristics associated with cryptocurrencies, through case law, a more cohesive understanding and categorisation can be achieved to further understand this technology and observe how regulations can either apply or be modified to apply to crypto assets as a whole.

Furthermore, each regulatory body, has contributed their own understanding of how a cryptocurrency may be perceived, therefore influencing the manner in which the regulatory bodies may exert their authority in regulating cryptocurrency.

b) Securities and Exchange Commission (SEC)

The SEC is a federal regulatory body that aims to ensure the protection of investors, the facilitation of capital and lastly, a fair, structured and efficient functioning of the financial market in the USA. This is achieved by controlling the activities associated with securities and investments,[50] through the implementation of a number of regulations.[51]

The SEC has indicated that it will have the authority to oversee and regulate any transaction that results in a cryptocurrency resembling a security or alternatively an investment contract.[52] In addition to this understanding, the SEC is understood to also have regulatory authority over ICO's.[53]

Hence, it is important to understand that the SEC would analyse the underlying nature of the transaction, to determine whether the cryptocurrencies associated with the said transaction can be deemed as a security. In order to complete this analysis, the SEC relies on the 'Howey Test'. This test

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[46] No. 15-1815 (2d Cir. 2017).
[47] *United States v Ulbricht, No. 15-1815 (2d Cir. 2017).*
[48] Case No. 4: 13-CV- 416 United States District Court.
[49] J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8; See also: L Sadhaseevan op cit note 8.
[50] A security refers to stocks, bonds and transferable shares. Furthermore, an investment contract is considered to be a security as well. J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8; See also: Section 2(a)(1) of the Securities Act of 1933.
[51] For an in-depth description of the relevant regulations please refer to: *https://www.investor.gov/introduction-investing/investing-basics/role-sec/laws-govern-securities-industry.*
[52] An investment contract is defined by the case of *SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946)*, which states that an investment of money in an enterprise must result in a reasonable expectation that profits will be derived from a third party of the enterprise. J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8; See also: L Sadhaseevan, op cit note 8.
[53] For further information on the treatment of ICO's refer to: 'Statement on Potentially Unlawful Online Platforms for Trading Digital Assets' *U.S. Securities & Exchange Commission* 2018, available at: *https://www.sec.gov/news/public-statement/enforcement-tm-statement-potentially-unlawful-online-platforms-trading*, accessed on 10 January 2021.

looks at the '…circumstances surrounding the digital asset and the manner in which it is offered, sold or resold (which includes the secondary market).'[54]

Therefore, platforms that are involved in the trading of cryptocurrency that fit the definition of a security, will be subjected to federal security regulations. By virtue of being subjected to security regulations, these platforms will be required to be registered with the SEC as a security exchange or qualify for an exemption to register as a security exchange, in order to be able to exchange these types of securities. Through registration, it will allow investors to make decisions that are informed, as these platforms facilitating securities would be required to make full disclosures of their operations to the SEC.[55]

Through the SEC, notices are issued to warn consumers of platforms that either did not qualify for exemption or be registered with the SEC for the trade of securities. Furthermore, the SEC would place these companies/platforms on a blacklist, resulting in these companies not being able to trade securities.[56] Hence it can be noted that if a crypto asset is sold as a security, it would be regulated by the SEC.

c) Commodities and Futures Trading Commission (CFTC)

The CFTC regulates the derivative market[57] found within the USA. The CFTC is underpinned by the Commodity Exchange Act 1936 (CEA). Through the CEA, the CFTC protects the public against abusive practices related to derivative products and other products associated with the CEA.[58]

In terms of the CEA, it has been found that cryptocurrencies are deemed to be commodities. A commodity is defined in terms of section 1a (9) of the CEA. Through this section, commodities are identified as being all services and rights associated with intangible products and goods and services associated with tangible products in relation to specifically contracts for future delivery, and are dealt with in the present or in the future.[59]

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[54] 'Framework for "Investment Contract" Analysis of Digital Assets' *U.S. Securities & Exchange Commission*, available at: *https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets*, accessed on 10 January 2021.

[55] Ibid; See also: 'Statement on Potentially Unlawful Online Platforms for Trading Digital Assets' op cit note 53.

[56] The SEC may also take companies/platforms that flout securities regulations to Court. An example of this is the action that has been filed by the SEC against Ripple Labs Inc, a company that raised $1.3 billion through its digital token known as XRP. The SEC viewed this token as an unregistered asset security, as the company did not register itself with the SEC prior to offering a security in the form of the cryptocurrency. R Huang 'What the SEC Charging Ripple Means For Cryptocurrencies; *Forbes* 2020, available at: *https://www.forbes.com/sites/rogerhuang/2020/12/23/what-the-sec-charging-ripple-means-for-cryptocurrencies/?sh=77eb51233bd3*, accessed on 19 January 2021. For further information and examples of companies the SEC has identified on their watchlist, refer to: D Nelson 'SEC Calls Out Suspicious Crypto Companies Targeting Global Traders' *Coin Desk* 2021, available at*: https://www.coindesk.com/sec-adds-bogus-crypto-firms-watchlist*, accessed on 25 January 2021.

[57] The derivative market refers to commodities such as futures, options and derivative contracts; For more information please see: *https://cointelegraph.com/explained/derivatives-in-crypto-explained*.

[58] Commodity Futures Trading Commission *A CFTC Primer on Virtual Currencies* (2017).

[59] Ibid.

Furthermore, the classification of a cryptocurrencies being classified as a commodity is further confirmed in the case of *Coinflip, Inc., d/b/a Derivabit, and Francisco Riordan, CFTC*,[60] it was stated that Bitcoin and other cryptocurrencies are encompassed within the definition of a commodity. As stated by Lucking and Aravind,[61] through the CFTC, anti-fraud practices will therefore, also apply to the trade of crypto assets by virtue of it being considered a commodity.[62]

Therefore, it must be noted that the CFTC will only have regulatory authority over cryptocurrency, when it is used as a derivative, or if there is fraud, manipulation or abusive practices involved in the *trade* of cryptocurrencies.[63]

In order to determine whether a cryptocurrency falls within the CFTC's jurisdiction, the CFTC will look at the circumstance in which the cryptocurrency is used. This is a similar approach used by the SEC.[64] This means the CFTC will look at whether a cryptocurrency is being utilised in terms of the meaning of 'commodity' as found within the CEA, in order to establish its jurisdiction.[65]

d) Financial Crimes Enforcement Network (FinCEN)

FinCEN is a body tasked with protecting the financial system of the USA against money laundering and the funding of terrorism. This particular authority has issued guidance on regulations relating to money transmission and anti-money laundering in terms of money services business. According to Dewey, FinCEN would regulate the following money service businesses in relation to cryptocurrency:[66]

1. Virtual asset exchanges; and
2. Entities that function as an authority to redeem and issue crypto assets.

Furthermore, the definition of a money transmitter is further widened to encompass activities of cryptocurrencies, whereby: 'An administrator or exchanger that (1) accepts and transmits a convertible virtual currency or (2) buys or sells a convertible virtual currency for any reason is a money transmitter…'[67]

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[60] Docket No. 15-29.3.
[61] D Lucking & V Aravind 'Cryptocurrency as a Commodity: The CFTC's Regulatory Framework' 2020 *Global Legal Insight*.
[62] J Dewey 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8; See also: Commodity Futures Trading Commission *A CFTC Primer on Virtual Currencies* (2017).
[63] Commodity Futures Trading Commission *A CFTC Primer on Virtual Currencies* (2017).
[64] Ibid.
[65] Refer to: *https://www.jdsupra.com/legalnews/cftc-jurisdiction-over-cryptocurrency-99573/,* for further information on the CFTC jurisdiction.
[66] Commodity Futures Trading Commission *A CFTC Primer on Virtual Currencies* (2017).
[67] Department of Treasury Financial Crimes Enforcement Network *Application of FinCEN's Regulations to Persons Administering, Exchanging or Using Virtual Currency,* FIN2013G001,2013; See also: J Dewey, 'Blockchain Cryptocurrency Regulation 2021—USA' op cit note 8.

The implication is that money transmission and anti-money laundering laws will apply to money service businesses who engage in activities that are concerned with cryptocurrencies. In addition, all money service businesses must implement a program to ensure AML/CTF is achieved.[68]

In 2013, FinCEN released a guidance that confirmed the applicability of the Bank Secrecy Act of 1970 in relation to cryptocurrency transactions.[69]

Through this guide, it was established that should a person or company fall within the definition of a money transmitter, and engage in activities associated with cryptocurrency, then the BSA would be applicable against such entities.[70]

The Bank Secrecy Act[71] is a piece of legislation that is relied upon by the FinCEN to ensure AML/CTF is achieved.[72]

To further bolster regulations to promote AML/CTF, the FinCEN in 2019 released a guidance that included a travel rule[73] in relation to virtual currency. This travel rule was largely similar to that recommended by the FATF, however differed in terms of the transaction thresholds.[74] Hence, when a transfer is affected between money service businesses, on behalf of a client, and the transaction exceeds the transaction threshold, the travel rule will be applied.[75]

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[68] Ibid.

[69] Department of Treasury Financial Crimes Enforcement Network *Application of FinCEN's Regulations to Persons Administering, Exchanging or Using Virtual Currency,* FIN2013G001,2013.

[70] Ibid.

[71] Bank Secrecy Act of 1970.

[72] The application of this act is as follows:

- Users of cryptocurrencies that engage in making payments and purchases do not fall within the ambit of the act and are therefore not a money service business.
- The act will be applicable to exchanges and those parties who exchange cryptocurrencies for other crypto assets, or exchange crypto assets for legal tender.
- Individuals and businesses who use cryptocurrencies for their own purpose and not for the interest of another is not considered as being a money service business. This also includes mining for one's own purpose.
- Mining for one's own purpose, as well as cloud mining are not considered being a money service business.
- Trading platforms engaged in activities involving in the selling of cryptocurrencies are required to comply with the act.
- Payment systems used by sellers, that reive cryptocurrencies as a form of payment must comply with act.

Department of Treasury Financial Crimes Enforcement Network *Application of FinCEN's Regulations to Persons Administering, Exchanging or Using Virtual Currency,* FIN2013G001,2013; See also: 'The Bank Secrecy Act & Cryptocurrency' *Davitian Law*, available at: *https://www.davitianlaw.com/cryptocurrency-defense/bank-secrecy-act/*, accessed on 19 January 2021.

[73] In terms of the travel rule, this is found within recommendation 16 of the FATF, and the purpose of this recommendation is to prevent terrorists and other criminals from having unregulated access to move their funds through the use of wire transfers. For further information: *https://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf*.

[74] According to the 2019 guidance, the threshold for transaction was marked at $3000. However, a further guidance, that is still open for comment was released in 2020 and proposes that the new threshold of $250. This threshold is in stark contrast to the FATF threshold of $1000.

[75] For further information on the travel rule, please refer to chapter 4. See also: Department of Treasury Financial Crimes Enforcement Network *Guidance Application of FinCEN's Regulations to Certain Business Models Involving Convertible Virtual Currencies*; See also: 'Guidance for a Risk-Based Approach to Virtual Assets and Virtual Asset Service Providers' *FATF* 2019, available at*: http://www.fatf-gafi.org/publications/fatfrecommendations/documents/guidance-rba- virtual-*

A further Notice of Proposed Rule Making (NPRM) was released in October 2020, regarding the travel rule by FinCEN. FinCEN furthermore released a NPRM in December 2020.[76] This NPRM dealt with procedures relating to recordkeeping and reporting requirements that occur between financial institutions and money service businesses and crypto asset wallets. This NPRM proposes that new rules be applied in relation to money service businesses transactions involving cryptocurrencies.[77]

The proposed rules aim to ensure there is greater recording of details between money service businesses and cryptocurrency wallets. This information hence, has to be submitted to FinCEN upon transaction thresholds being breached.

e) Future Legislation

This *Cryptocurrency Act of 2020* is a Bill that was announced in 2020 (Bill). This Bill serves to simplify the understanding of cryptocurrencies, under a single piece of legislation. The purpose of this Bill is to ensure there is a regulatory response given towards cryptocurrencies. Such information may include knowledge about licences, or certifications.[78]

Through this Bill, it is important to note, that a definitional understanding is provided in relation to cryptocurrencies, at a Federal Level. Currently, the Federal government does not have a unified definition of what constitutes as a cryptocurrency. This has resulted in various regulatory bodies defining a cryptocurrency in accordance with their own regulations.

This Bill creates a unified understanding and approach as to what constitutes a cryptocurrency. Within this act, the umbrella term known as 'digital asset' is utilised, as opposed to the term cryptocurrency. A digital asset encompasses subsets known as: 'crypto-currency',[79] 'crypto-

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assets.html, accessed on 20 January 2021; K Kirkpatrick, K Telep, S Das & J Gerber 'FinCEN 'Travel Rule' Update Sets Challenges for Crypto' 2019 *Cos Law* 360.

[76] For further reading, please refer to: Department of Treasury Financial Crimes Enforcement Network *Requirements for Certain Transactions Involving Convertible Virtual Currency or Digital Assets* 2020.

[77]These rules relate to the following: 'to submit reports, keep records, and verify the identity of customers in relation to transactions involving convertible virtual currency (CVC) or digital assets with legal tender status ('legal tender digital assets,' or 'LTDA') held in wallets not hosted by a financial institution ('unhosted wallets') or wallets hosted by a financial institution in FinCEN identified jurisdictions.'

L Zirogiannis 'FinCEN Announces Proposed Rule Aimed at Closing Anti-Money Laundering Regulatory Gaps for Certain Convertible Virtual Currency and Digital Asset Transaction' (2021) 11 *The National Law Review*; See also: Department of Treasury Financial Crimes Enforcement Network *Requirements for Certain Transactions Involving Convertible Virtual Currency or Digital Assets.*

[78] K Helms 'US Lawmaker Introduces Crypto-Currency Act of 2020 While Under Coronavirus Quarantine' *Bitcoin* 2020, available at: *https://news.bitcoin.com/cryptocurrency-act-of-2020/*, accessed at 20 October 2020; See also: 'What is the Crypto-currency Act of 2020' *Sygna* 2020, available at: *https://www.sygna.io/blog/what-is-cryptocurrency-act-of-2020/*, accessed on 15 December 2020.

[79] The term 'crypto-currency' means representations of United States currency or synthetic derivatives resting on a blockchain or decentralised cryptographic ledger, including:

(A) such representations or synthetic derivatives that are reserve-backed digital assets that are fully collateralised in a correspondent banking account, such as Stablecoins; and

(B) synthetic derivatives that are:

(i) determined by decentralised oracles or smart contracts; and

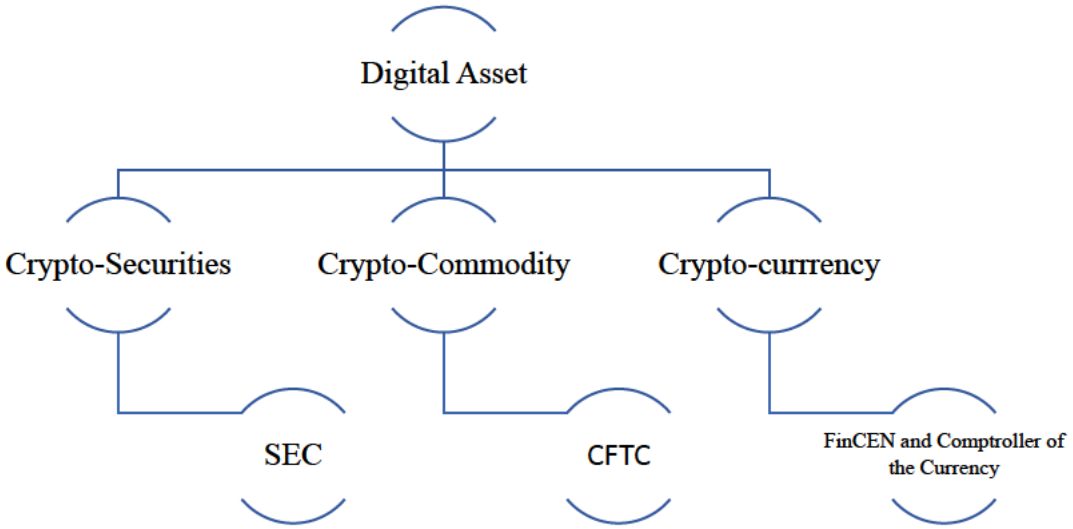
(ii) collateralised by crypto-commodities, other crypto-currencies, or crypto-securities.

commodity'[80] and 'crypto-security'[81]. Hence, through this Bill, a holistic understanding of cryptocurrency is created at a Federal level, whereby a cryptocurrency is seen as a subclass within a digital asset, similar to how a crypto asset is perceived in South Africa and the UK.[82]

Furthermore, through the definitions provided above, each subset of digital asset will then be subjected to the relevant regulatory body, who is assigned to deal with the respective digital asset subset as its sole authority.[83] Hence, 'crypto-currency' is regulated by FinCEN and the Comptroller of the Currency, 'crypto-commodity' is regulated by the CFTC, and 'crypto-security' is regulated by the SEC. Each regulatory body is further defined in the Bill.[84]

A summary of how digital assets are categorised and regulated by respective regulatory bodies can be found bellow:

Figure 1



This definition is derived in terms of section 2(3) of the Cryptocurrency Act of 2020.

[80] The term 'crypto-commodity' means economic goods or services, including derivatives, that:
(A) have full or substantial fungibility;
(B) the markets treat with no regard as to who produced the goods or services; and
(C) rest on a blockchain or decentralised cryptographic ledger.
This definition is derived in terms of section 2(1) of the Cryptocurrency Act of 2020.

[81] The term 'crypto-security' refers to all debt and equity that rest on a blockchain or decentralised cryptographic ledger. However, the exception is that it does not include a synthetic derivative that:
(I) is operated as, and is registered with the Department of the Treasury as, a money services business (as defined under section 1010.100 of title 31, Code of Federal Regulations); and
(ii) is operated in compliance with all applicable requirements of subchapter II of chapter 53 of title 31, United States Code (commonly referred to as the 'Bank Secrecy Act') and all other Federal anti-money laundering, anti-terrorism, and screening requirements of the Office of Foreign Assets Control and the Financial Crimes Enforcement Network.
This definition is derived in terms of section 2(3) of the Cryptocurrency Act of 2020.

[82] K Helms 'US Lawmaker Introduces Crypto-Currency Act of 2020 While Under Coronavirus Quarantine' op cit note 78; See also: 'What is the Crypto-currency Act of 2020'op cit note 78.

[83] Ibid.

[84] Ibid; For further information, please refer to the Crypto Currency Act of 2020.

This Bill also delves further in defining and describing different types of Stablecoin,[85] which is relevant, considering the emergence of Stablecoins. Consequently, this Bill delves beyond digital assets, and looks at the regulation of smart contracts[86] as well.

Furthermore, this Bill provides provisions on the registration and public lists of cryptocurrency exchanges and the requirements to create or trade in cryptocurrency.[87]

The Bill also ensures that the regulators maintain regulation of their respective categories by making it necessary for authorities to keep records of licenses, registrations and certificates required for the trade of cryptocurrencies. Furthermore, through this Bill, the transactional path of cryptocurrencies can be tracked.[88]

It must however be noted, that at the time of writing, this Bill is yet to be passed to become Federal law. Hence, this Bill, provides the potential for a greater understanding into the regulation of cryptocurrencies. Furthermore, it places responsibility on the regulatory bodies to regulate cryptocurrencies by providing guidance through a foundational form of legislation that can be relied upon by regulators.

IV. CONCLUSION

Through an analysis of the UK and USA respectively, it can be said that there are various similarities that are present between these foreign jurisdictions and South Africa. Such similarities can be found in terms of the AML/CTF provisions found within both countries. The reason for this is because all jurisdictions are guided by the FATF, hence jurisdictions will apply similar regulations.

Furthermore, USA, at a federal level relies on various regulatory bodies to interpret and regulate crypto assets. This is similar to the approach also utilised by South Africa. Contrasting this however, is the UK that utilises the FCA as its sole authority in relation to crypto assets.

The UK and South Africa however a similar understanding by adopting the collective term crypto asset. However, contrasting South Africa, the UK further categorises a crypto asset as being associated with e-money and securities. This is a useful observation that South Africa can adopt in further

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[85] According to the Crypto Currency Act 2020, there are reserve-backed Stablecoin and synthetic Stablecoin. In addition, it must be noted that a further bill has been proposed known as the Stablecoin Act, that would aim to ensure the efficient regulation of Stablecoins within the USA. The Stable Act would apply to cryptocurrency that has the 'reasonable expectation or belief among the public that the instrument will retain a nominal redemption value'. P. J. Boot 'New Legislation Proposes to Merge Crypto and Banking' *The National Law Review* 2021, available at: *https://www.natlawreview.com/article/new-legislation-proposes-to-merge-crypto-and-banking*, accessed on 20 February 2021; See also: 'What is the Crypto-currency Act of 2020' op cit note 78.

[86] A smart contract refers to a contract based on computer code. This computer code automatically will execute either all or partial parts of the contract. Furthermore, the contract is stored on blockchain technology. D Stuart & A Lipton 'An Introduction to Smart Contracts and Their Potential and Inherent Limitations' *Harvard Law School Forum on Corporate Governance* 2018, available at: *https://corpgov.law.harvard.edu/2018/05/26/an-introduction-to-smart-contracts-and-their-potential-and-inherent-limitations/*, accessed on 15 December 2020.

[87] 'What is the Crypto-currency Act of 2020' op cit note 78.

[88] Ibid.

developing their definition and understanding of a crypto asset to encompass both e-money and securities. By virtue of this, legislation that applies to e-money and securities will then apply to crypto assets that can be categorised as e-money and a security, and therefore applicable towards cryptocurrencies.

South Africa can also further also adopt legislation similar to the Cryptocurrency Act of 2020. Through the structure of this Bill, it can be observed that it provides a foundational understanding as to the specific regulatory bodies that would have authority over a cryptocurrency Should South Africa implement such a form of regulation, it would aid in ensuring that regulatory authorities have a common understanding of crypto assets and what it constitutes, thereby eliminating any confusion as to whether a specific regulatory body may or may not have authority over regulating crypto assets.

It can further be observed that South Africa's international counterparts are evolving their existing regulation in line with technology, to ensure that there is a comprehensive network of regulations available at their disposal to prevent any illegal activities concerning crypto assets.

Hence, in conclusion it can be noted that through these two jurisdictions, South Africa can learn and adopt certain aspects of their respective regulation to ensure there is a comprehensive form of regulation available in respect to crypto assets, and therefore cryptocurrency.

CHAPTER 6
RECOMMENDATIONS AND CONCLUSIONS

I. CHAPTER OVERVIEW

The main objective of this research is to provide an analysis on regulations in relation to crypto assets within South Africa. The previous chapters provided an opportunity to analyse the current legislative landscape in relation to crypto assets within South Africa and internationally. Through this analysis, an crypto asset technology is better understood, and the definition of a crypto asset and how it can be potentially regulated is determined.

Through this chapter, a summary of the findings researched will be provided, and consequently, further recommendations in regulating cryptocurrencies within South Africa will be proposed. These further recommendations will be in addition to existing recommendations that have been proposed by policy papers and international jurisdictions such as the UK and USA.

II. FINDINGS

A crypto asset is seen to challenge traditional forms of financial regulations. The reason for this challenge is due to the fact that crypto assets are not considered to be a form of legal tender, although it exhibits characteristics similar to that of a legal tender. Hence, this result in transactions involving crypto assets to circumvent regulations put into place to prevent the abuse of the financial sector.

Therefore, through the introduction of crypto assets, it has allowed regulatory bodies to debate and analyse this new form of Fintech and determine how cryptocurrencies can effectively and efficiently be regulated.

Hence, in terms of chapter 2, the technology that underpins crypto asset were analysed to determine the characteristics and uses of crypto assets. Furthermore, chapter 2 provided definitional clarity of what constitutes a crypto asset. It was determined that a cryptocurrency is a subset found within the collective term known as a crypto asset. Within South Africa, crypto assets further encompass exchange tokens (cryptocurrency), ICO's, security tokens. Crypto assets are also seen as pseudonymous, encrypted and based on blockchain. Hence, transactions involving crypto assets are therefore not dependant on third parties such as banking institutions. Furthermore, such transactions, also makes it easier for parties to a crypto asset transaction to circumvent financial regulation laws by virtue of being pseudonymous.

Chapter 3 provided an analysis of the three position papers concerning the stance taken by regulatory bodies in relation to cryptocurrencies. It can be noted that in terms of the 2014 Position Paper, it merely provided a warning of the risks associated in dealing with cryptocurrencies. In terms of the

2019 Consultation Paper, a focus was given primarily on the AML/CTF provisions, as recommended by the FATF. However, in terms of the 2020 Position Paper, it built on the lessons of past policy papers and provided thirty recommendations that encompassed AML/CTF recommendations as well as recommendations dealing with market regulation and cross border transactions.

In addition, this chapter illustrated the dynamic view regulators had in developing the definition and progressing from the term cryptocurrency to a collective term known as crypto assets. Presently as it stands, the term crypto asset is preferred as it encompasses the characteristic of an 'asset' as opposed to a 'currency' creating a more accurate term to be used.

In terms of chapter 4, this particular chapter provided an analysis of financial regulations in relation to crypto assets. In performing this analysis, relevant regulations pertaining to crypto assets were identified within the PA and FSCA. It can be determined that the Banks Act and SARB Act of the PA do not apply to cryptocurrency. However, the in terms of the FSCA, in conjunction with recommendations made by the policy papers, the legislation identified were seen to apply towards the regulation of crypto assets. However, it must be noted that the FSCA would only be able to regulate crypto assets once the actual regulations are amended.

As it stands, in the current dispensation, no regulatory body actually has any authority to regulate crypto assets. Furthermore, Exchange Control Regulations were also analysed. It was determined that there are frameworks in place that would allow for the monitoring of legal tender used to by offshore crypto assets, however these monitoring capabilities are hindered by the fact that SARB does not recognise crypto assets within its framework. Hence, this impedes regulation of offshore transactions.

Through this chapter it can noted that there is the intention on behalf of regulatory bodies to modernise themselves to ensure there is regulation of cryptocurrencies within the financial sector, however there needs to be a more concentrated effort between regulatory bodies, whereby cryptocurrency regulation must not be seen in isolation but be seen in conjunction.

In terms of chapter 5, this chapter provided an analysis of crypto asset regulations found within the UK and USA. Within this chapter, it can be noted that the UK and South Africa share similarities in the manner in which crypto assets are regulated, especially in terms of AML/CTF regulations. Furthermore, both countries make use of the collective term 'crypto asset', which has various subsets such as tokens, and cryptocurrencies to name a few.

However, compared to South Africa, the UK views both e-money and securities falling within the ambit of a crypto asset, therefore allowing for greater through legislation relating to e-money and securities. Hence, South Africa can further analyse the UK's approach, and determine whether e-money should be included within the ambit of crypto asset. Furthermore, the UK has a robust definition of what

is regulated and unregulated crypto assets, based on a crypto assets category. This is another aspect of UK law that South Africa can apply to further understand how crypto assets can be regulated.

Contrasting the UK, the USA has a robust Federal level regulation in relation to cryptocurrencies. The USA utilises various Federal regulatory, who have interpreted cryptocurrencies to fall within their required definitions and therefore their respective authorities. This has resulted in cryptocurrencies being recognised as being a security as well as a commodity.

In order to achieve this inclusion, regulatory bodies relied on case law to further understand how crypto assets may be understood in relation to existing regulations. Furthermore, the USA, like South Africa applied relevant AML/CTF regulations in relation to crypto assets. However, in addition to regulatory bodies, the USA has drafted a bill that looks at the creation of a single act known as the Cryptocurrency Act of 2020.

This Act aims at regulating cryptocurrencies in relation to its relevant subset found within the collective term 'digital asset', a similar concept to the term 'crypto asset' as used by the UK and South Africa. According to the specific digital asset subset, a corresponding regulatory body would have the sole authority to regulate the respective digital asset subset. However, this bill is yet to be made law.

Hence, it can be seen through analysing the UK and USA, South Africa can utilise a similar manner to these two countries to further understand the nature of crypto assets and further develop efficient yet effective regulations in relation to crypto assets. Hence, this chapter provides more clear recommendations as to how South Africa may adapt its legislation.

III. RECOMMENDATIONS

Through the 2019 Consultation Paper and 2020 Position Paper, various recommendations were advanced to ensure the adequate regulation of cryptocurrency within South Africa. Many of these recommendations dealt with ensuring AML/CTF compliance in accordance with the FATF regulations. In addition, regulations found in the UK and USA, as well as policy papers can be utilised to conceive further recommendations for crypto asset regulation.

a) Conduct of Financial Institutions Bill (COFI Bill)

Through the Twin Peaks model, further development has been made,[1] leading to the introduction of the COFI Bill.[2] This bill was drafted for the FSCA, in relation to financial institutions and their respective conduct requirements. Through the COFI Bill, market regulation found within the FSCA will be integrated, addressing the lacunae that exists between market regulation.[3]

As indicated by Govender, the COFI Bill has the general objective of ensuring fair treatment of customers, financial inclusion, competition and transformation within the market.[4] In addition to these objectives, it is further stated in terms of Clause 3 of the COFI Bill that one of the aims is to 'promote investment and the development of an investment in innovative technologies, processes and practices'.[5] This clause serves as an indicator that the COFI Bill intends to provide for regulation in terms of Fintech.[6] Although the COFI Bill does not make direct reference to regulating crypto assets, it can be inferred that the COFI Bill aims to regulate crypto assets, by virtue of crypto assets falling within the scope of Fintech.[7]

Govender further notes that the COFI Bill utilises an activity-based approach with regards to Fintech. This activity-based approach will aid in development of legislation to regulate crypto assets based on the relevant activity associated with the respective crypto asset.[8]

In relation to crypto assets, as noted in the 2020 Position Paper,[9] it was recommended that CASPs administering services in relation to crypto assets be included within the ambit of the concept 'licensing activities', found within the Conduct of Financial institutions Bill (COFI Bill).[10]

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[1] Through the FSCA, a paper entitled *the Regulatory Strategy of the FSCA: October 2018 to September 2021* was published. Within this paper, the FSCA highlighted that through the introduction of crypto assets within the financial sector of South Africa, the gaps in financial regulation have been emphasised. In light of this, the FSCA has proposed that regulations to regulate crypto assets should be principle based, activity centred and technology neutral. Therefore, it is further acknowledged by the FSCA, that if a crypto asset is to be associated with financial services, then, such crypto assets must be regulated to ensure fair market practices as well the fair treatment of customers. See also: Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group *Consultation Paper on Policy Proposals for Crypto* (2019); Financial Sector Conduct Authority *Regulatory Strategy of the Financial Sector Conduct Authority* (2018); L Sadhaseevan *The Regulation of Crypto Currency in The Context Of South Africa's Financial Sector* UKZN (2020) at 94.

[2] The first draft of the COFI Bill was published in 2018, with the second draft of the COFI Bill being published in 2020.

[3] G Fry, 'New PPR Rules in Regulatory Reform' (2017) 2017 *Money Marketing* at 6; See also: K Hanekom 'Will COFI Act be Effective in Regulation of Commercial Umbrella Funds?' (2019) 2019 *Money Marketing* 8.

[4] S Govender 'A Fintech Take in the Conduct of the Financial Institutions Bill' (2019) 19 *Without Prejudice* 2.

[5] Clause 3 of the COFI Bill; See also: S Govender 'A Fintech Take in the Conduct of the Financial Institutions Bill' op cit note 4.

[6] S Govender 'A Fintech Take in the Conduct of the Financial Institutions Bill' op cit note 4.

[7] Refer to chapter 2 for an explanation into the technological foundation of crypto assets, and its relation to Fintech.

[8] S Govender 'A Fintech Take in the Conduct of the Financial Institutions Bill' (2019) op cit note 4.

[9] Refer to chapter 3, Section I as well as Section IV for an in-depth analysis of the 2020 Position Paper.

[10] Intergovernmental Fintech Working Group Crypto Assets Regulatory Working Group Position Paper on *Crypto Assets* (2020) at 9.1.2.1, Recommendation 9; 23 and 29.

b) Definitional Clarity

Definitional clarity is important to have with regards to cryptocurrencies. Without a definitional clarity, regulators will not be able to determine if the concept of a crypto asset and its respective subclass, a cryptocurrency will fall within its ambit of authority. By having definitional clarity, it would allow regulators to avoid any confusion or conflicting perspectives, as found in terms of the Exchange Control Regulations and SARB, and further allow regulators like SARS to apply a uniform definition when making legislation.

Furthermore, South Africa should continue to improve on the definitions of crypto assets to include Fintech such as e-money and Stablecoins within the ambit of 'crypto assets' – much like how the UK developed their understanding of crypto assets. This would allow for more financial regulations to apply in regulating crypto assets. Hence, it is important for regulatory bodies to continue developing and understanding the definition of a crypto asset to ensure applicability of regulations.

c) Cryptocurrency Legislation

South Africa should also consider working towards developing their own version of a form of legislation that governs crypto assets, and cryptocurrencies as a whole, similar to the Cryptocurrency Act of 2020. By having a single piece of legislation, it may allow for greater clarity as to how regulatory bodies may regulate cryptocurrencies. Through such a legislation, it would define specific regulatory bodies, who would regulate a specific crypto asset category, as allowed by the regulatory bodies mandate. Furthermore, by having such an act, it may allow for greater harmonisation between the regulatory bodies, and therefore contributing to greater definitional clarity. Hence, regulatory bodies would not be seen in isolation from one another, but instead seen as a structured network of authorities that regulate cryptocurrencies. Through this 'legislation' it can also aide to achieve definitional clarity by providing a uniform definition that regulatory bodies may rely on.

In addition to creating crypto asset legislation, South Africa can amend existing legislation to ensure that crypto assets are regulated. An example of this can be found in terms of FICA, whereby it can be amended to ensure that CASPs fall within the definition of an 'accountable institution' as found in Schedule 1 of FICA. Furthermore, as noted in chapter 4, the FSCA would only be able to regulate crypto assets once the actual regulations are amended. Furthermore, the FSCA mainly relates to regulating crypto assets via CASPs. Hence, it can be observed that the FSCA regulates the services associated with crypto assets through CASPs rather than the crypto asset itself.

IV. CONCLUSION

Therefore, it can be said that in terms of this dissertation, that a cryptocurrency is a sub-class found within the collective term of a crypto asset. Crypto assets are seen as being decentralised convertible virtual currencies that are pseudonymous, and are underpinned by blockchain technology, that allow for its decentralised nature.

Through the characteristics of crypto assets, it allows for the circumvention of existing financial regulations within South Africa as many regulations pre-dates the existence of crypto assets. Therefore, regulators in South Africa should ensure that there is some form of definitional clarity and uniformity between regulators, to reduce confusion and ensure that there is efficient regulation of crypto assets.

Hence through the recommendations, amendments can be made as required to ensure the efficient regulation of crypto assets. However, it must be understood that the current findings pertain to crypto assets being dealt with in conjunction with a legal tender and services offered by CASPs. Hence, if there is a crypto asset transaction that involves the exchange or purchase of legal tender, then the potential amended legislation will apply.

However, if a crypto asset is dealt with solely, where no legal tender is involved in the transaction, it will result in full pseudo-anonymity of parties. Therefore, this results in regulations not being applicable. Hence, the existing understanding of potential crypto asset regulations rests on the idea that legal tender would be used in some way or the other in a crypto asset transaction. Furthermore, should the crypto asset transaction not fall within the services of a CASP, FSCA regulations will also not apply.

Therefore, regulatory bodies would need to continue to further study and understand crypto assets in order to develop comprehensive legislation, as found in the UK and USA. In addition, regulatory bodies in South Africa have merely proposed recommendations and bills that are not law. Furthermore, these recommendations aim to regulate the services associated with crypto assets rather than the concept of crypto assets solely.

Hence, as it stands, no regulatory body has the authority to regulate crypto assets. However, this may change in the future, but as it stands, crypto asset use exemplifies its decentralised nature and the need for regulatory reform.

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UNIVERSITY OF KWAZULU-NATAL
INYUVESI YAKWAZULU-NATALI

Mr Kyavand Gholizadeh Touchaei (216048355)
School Of Law
Howard College

Dear Mr Kyavand Gholizadeh Touchaei,

Protocol reference number: 00007873
Project title: AN ANALYSIS OF CRYPTOCURRENCY REGULATION WITHIN SOUTH AFRICA AND THE IMPACT THAT CRYPTOCURRENCY HAS ON EXISTING FINANCIAL REGULATIONS.

Exemption from Ethics Review

In response to your application received on 19/08/20 , your school has indicated that the protocol has been granted **EXEMPTION FROM ETHICS REVIEW.**

Any alteration/s to the exempted research protocol, e.g., Title of the Project, Location of the Study, Research Approach and Methods must be reviewed and approved through an amendment/modification prior to its implementation. The original exemption number must be cited.

For any changes that could result in potential risk, an ethics application including the proposed amendments must be submitted to the relevant UKZN Research Ethics Committee. The original exemption number must be cited.

In case you have further queries, please quote the above reference number.

PLEASE NOTE:
Research data should be securely stored in the discipline/department for a period of 5 years.

I take this opportunity of wishing you everything of the best with your study.

Yours sincerely,

[redacted]

Mr Simphiwe Phungula
Research and Higher Degrees Committee
School of Law