EUROMONEY

BitLicense not template for UK, say experts

While accepting that regulation can help increase consumer and business confidence in cryptocurrencies, providers and industry analysts agree that the BitLicense model is not the way forward for the UK

Paul Golden

December 1, 2016

The European Commission’s proposed directive amending the Fourth Anti-Money Laundering Directive (4AMLD) proposes bringing virtual currency exchanges and custodian wallet providers into the scope of anti-money laundering and countering financing of terrorism legislation by adding those businesses to the list of 'obliged entities’.

The European Commission is also considering applying the licensing and supervision rules of the revised Payment Services Directive (PSD2) to digital currency exchanges.

The current proposals are vague and much needs to be done, including classifying digital currencies. However, if cryptocurrency is treated as mainstream money remittance under PSD2, user confidence is likely to grow, says Reed Smith financial services regulatory partner Jacqui Hatfield, adding that "it is difficult to see how it can be a viable mainstream option without regulation."

These measures would go some way towards providing financial institutions with regulatory certainty and comfort in their dealings with regulated virtual currency businesses, suggests Sian Jones, founder of public policy platform the European Digital Currency and Blockchain Technology Forum.

In time, consumer protection policy will be developed and legislation introduced to govern virtual currency intermediaries, while regulation covering integrity, security, solvency and segregation of funds will become part of the virtual currency landscape, adds Jones. "The UK government favours industry-led, self-regulation," she explains. "The European Banking Authority would like to see regulated governance authorities for each virtual currency, but this is a long way off."

Melanie Swan, founder of the Institute for Blockchain Studies (an independent, non-profit research institute that examines the implications of blockchain technology) agrees that regulatory clarity would increase business willingness to invest in cryptocurrency projects, although she suggests that consumer confidence is more likely to be boosted by trusted providers such as consumer banks implementing applications.

Philippe Gelis, CEO of FX management solutions provider Kantox, cautions that usage will not become widespread unless central banks build and back crypto fiat currencies (currencies that governments have declared to be legal tender, but are not backed by a physical commodity).

Regulatory overkill?

Clarity on future regulation would give businesses and consumers some sense of how to conduct their own affairs in a cryptocurrency economy, but authorities should be wary of hyper-regulation. Too much regulation in a disruptive environment like that of the digital currency arena could have a negative impact, completely stripping away its inherent benefits, says digital currency LEOcoin’s founder Dan Andersson.

He goes on to suggest that the terms of the BitLicense introduced by the New York Department of Financial Services in August 2015 negate one of the key features of cryptocurrency: that digital currency transfers are conducted anonymously on a public ledger maintained by a peer-to-peer network, maintaining privacy while ensuring transparency.

"Enforcing a stringent framework on the digital currency industry, requiring it to record the personal details of users, monitor their activity and retain that information for several years, feels like a retrograde step," he continues. "Furthermore, setting the resources needed to obtain a licence too high serves to drive illegal activity underground and either stifle innovation or force it elsewhere." Jim Harper, a senior fellow at Washington-based think tank the Cato Institute goes even further, suggesting that the experience of the BitLicense proves that regulation produces certainty in theory better than it does in practice. He describes the licence as an ill-defined, hodgepodge of regulations that hinders innovation by driving up the cost of starting new businesses.

"The BitLicense did not create certainty about the rules of the road for bitcoin businesses in New York and it did not create an upwelling of bitcoin business activity," he says, observing that America’s financial capital appears to be ceding ground on financial innovation to London.

Jones agrees, stating that the BitLicense regime is unnecessarily wide-ranging and burdensome. "Only a tiny number of virtual currency businesses have applied for a BitLicense," she says. "It favours large players and has driven almost all virtual currency and many distributed-ledger technology start-ups out of New York State."

While Hatfield generally favours sensible regulation, she warns that the UK should not require licensing ahead of the EU. "Arbitrage will not be possible as the licence requirement becomes more widespread or if the EU/UK require providers of digital currency platforms who want to access their customers to comply with the relevant licensing requirement or have an equivalent regime," she concludes.