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The Regulation of Cryptocurrencies in South Africa

By

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Declaration

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Anri Lock

October 2021

Summary

Society is always moving forward and a large part of that is the advent of new technologies, such as cryptocurrencies. Cryptocurrencies are in use in almost every country in the world and has posed many regulatory issues for authorities, especially with the increased use thereof in recent years, despite extreme volatility in the market.

Cryptocurrencies can be referred to as virtual currencies, crypto assets or digital currencies. These cryptocurrencies can be centralised or decentralised, meaning that there is either a central issuing authority or not. Furthermore, they can be convertible or non-convertible, thus having the ability to be exchanged for legal tender or not. This innovation is based on blockchain technology, which makes use of a distributed ledger system. In layman's terms, it entails that every transaction is recorded on the blockchain by miners, using complex algorithms known as cryptography. Anyone can choose to be a miner and when a transaction is recorded on the blockchain, the miner is awarded with a small amount of cryptocurrency. Miners can also introduce new cryptocurrency "coins" into the system.

The inherent characteristics of this technology, accordingly, include anonymity of users, cross border operation and the lack of a central authority regulating it. These characteristics pose numerous risks to users and in future may even pose systemic risks such as disrupting the national payment system and necessitate economic interventions. South African authorities have recognised the need to regulate cryptocurrencies to mitigate these risks. South Africa's regulatory response is risk-based, and the approach has been neutral toward cryptocurrencies, monitoring the situation and intervening only where necessary.

This dissertation seeks to clarify how cryptocurrencies operate, what risks they pose, the South African response and how it compares to other countries' responses, the appropriateness of the regulations and how they may be improved in the future. It is trite that regulation is indeed needed if we are to suitably incorporate cryptocurrencies in our financial systems and the question this dissertation seeks to answer is the best way it can be done.

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This dissertation is dedicated to my father, who supports me in everything that I pursue, with unfaltering belief. It is an honour to be the daughter of someone who so highly values diligence, dedication and perseverance. I will never stop being grateful for the opportunities you have presented me with.

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Chapter 1:

Introduction

1.1 Background

South Africa started using fiat currency, coins and notes, in the 17th century.¹ The first coins, Dutch Guilders, were brought to South Africa in 1652 and the first notes, the Rix dollar, in 1782.² From there legal tender has evolved to the use of debit and credit cards and Electronic Fund Transfers between accounts held through commercial banks. It should be no surprise that a novel payment method appeared on the horizon, namely cryptocurrencies.

Cryptocurrency has become a buzzword, with Bitcoin, Ethereum and Ripple XRP regularly making news headlines. These cryptocurrencies allow for an innovative way to pay for goods and services by using blockchain technology.³ As cryptocurrencies become more popular, risks appeared on the horizon. Some of these risks, such as tax evasion, have already materialised and others, such as systemic threats, are still on the horizon.⁴ What has become clear is that the cryptocurrency landscape is in serious need of regulation. The inherent characteristics of cryptocurrency, such as anonymity and untraceable transactions, make it precarious to use for consumers and the volatility of the value attributed to these “currencies” makes investments equally risky.⁵

South Africa, as most countries, accordingly, started to regulate cryptocurrency and authorities are monitoring them in order to mitigate some of these risks. The regulation, however, has posed to be difficult due to the aforesaid characteristics coupled with the novelty of cryptocurrencies.

¹ <https://www.resbank.co.za/en/home/what-we-do/banknotes-and-coin/history-of-banknotes-and-coin> (accessed: 18 August 2021).

² <https://www.resbank.co.za/en/home/what-we-do/banknotes-and-coin/history-of-banknotes-and-coin> (accessed: 18 August 2021).

³ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 15.

⁴ 22-27.

⁵ 23-24.

1.2 Research problem

The first week of 2021 saw more than a trillion dollars' worth of cryptocurrencies in circulation, making it the world's fifth most circulated "currency".⁶ This is shocking when one considers the risks associated with cryptocurrencies and the various regulatory *lacunae* that exist around it.

This completely novel way of doing business, investing, making or receiving payments and capital raising has thrown regulators into the deep end. The risks are far-ranging and may be serious enough to completely circumvent the national payment system or any central authority. This dissertation sets out to analyse the current landscape and to investigate the current risks and measures taken to mitigate those risks by authorities.

The South African government has taken an active approach and created the Intergovernmental Fintech Working Group and within this, the Crypto Asset Regulatory Working Group to address the problems surrounding cryptocurrencies. This Group's reports are currently the most comprehensive and detailed proposals in South Africa and are the centre of the investigation.

1.3 Aim and objectives of the study

This dissertation's aim is to lay out the regulatory landscape of cryptocurrencies in South Africa and analyse same. The first step in doing this is to explore how cryptocurrencies operate, figuring out what their characteristics are and understanding the technology and different components surrounding the use of cryptocurrency. By understanding the operation and nature of cryptocurrencies, the regulations can be better understood. The current regulations are assessed, and inherent problems and risks are identified and explained. Thereafter international perspectives are given and finally suggestions and recommendations made on how the landscape may be improved.

The objectives of the study thus flow from the above. Firstly, it is important to ascertain where South Africa currently stands towards cryptocurrencies and what measures are currently proposed or already in place. The next objective is to identify the fissures that will cause problems and increase risks, which objective must be

⁶ <https://qz.com/1954555/all-the-worlds-crypto-is-now-worth-more-than-1-trillion/> (accessed: 21 August 2021).

satisfied before it is possible to recommend improvements. Finally, the last objective is to give recommendations and suggestions to address the issues surrounding cryptocurrencies. Together with the aforementioned objectives, international perspectives are also considered.

As will become evident, cryptocurrencies are here to stay and it is paramount that the correct approach is taken to integrate the technology with our current society. This dissertation aims to present the current setting, identify problems and solutions for the seamless integration of this innovation in South Africa's financial system.

Chapter 2:

The definition, history and operation of cryptocurrencies

2.1 Introduction

Cryptocurrencies, crypto assets, virtual currencies and digital currencies – these terms are all buzzwords, used synonymously or being closely related, which developed over the last decade, causing excitement for amateurs and seasoned traders and investors alike. A plethora of cryptocurrencies have been developed since 2009, the most notable being Bitcoin, Litecoin, Ethereum and Ripple XRP.⁷

The technology surrounding cryptocurrencies is complex and as such this chapter seeks to clarify what virtual currencies, cryptocurrencies and crypto assets are as well as their origin and current operation, which will lay the foundation for the risk identification and necessary regulatory intervention.

2.2 History of cryptocurrencies

Most stakeholders accept that cryptocurrencies came into existence in 2009, with Bitcoin being the pioneer currency.⁸ Bitcoin was created by Satoshi Nakamoto, which is believed to be a pseudonym for an individual or group of creators.⁹ After Bitcoin, copious other forms of cryptocurrencies quickly came into being and a massive new technological playground was created with many different uses.

The reasoning behind cryptocurrencies was to move away from central authorities who have all the power to issue and govern currencies (legal tender) and create an open-source system where peer-to-peer transactions take place, users are identified by only a digital signature and where proof-of-work is used to record a public history of all transactions, which prevents double-spending.¹⁰

Cryptocurrencies exponentially grew from 2009 to 2021, with users skyrocketing from an estimated 3,47 million in May 2015 to approximately 73,32 million in May

⁷ A Nieman “A Few South African Cents’ Worth on Bitcoin” (2015) 18 *PELJ* 1978-2010 1986.

⁸ D Erasmus & S Bowden “A Critical Analysis of South African Anti-Money Laundering Legislation with regard to Cryptocurrency” (2020) 41 *Obiter* 309-327 309.

⁹ A Nieman “A Few South African Cents’ Worth on Bitcoin” (2015) 18 *PELJ* 1978-2010 1986.

¹⁰ S Nakamoto “Bitcoin: A Peer-to-Peer Electronic Cash System” (2008) 1.

2021.¹¹ Despite the immense risks and volatility associated with using cryptocurrencies, this technology has grown immensely in a short span of time. Certain governments are recognising cryptocurrencies as legal tender and/or foreign currency and some even introduced their own virtual currencies into the economy.¹² These virtual currencies are evidently centralised, and initial coin offerings (ICOs) have sprung up as an alternative to venture capital.¹³

Due to the novelty of virtual currencies, the uses, risks and economic effects are still being discovered and evaluated. Most countries are attempting to regulate virtual currencies and especially the subgroup cryptocurrencies in order to mitigate the economic effects and risks associated with it, while still attempting to encourage innovation.

2.3 Definitions of cryptocurrencies and surrounding elements

Defining virtual currencies, cryptocurrencies and crypto assets has proven to be difficult, as even the terms and accompanying definitions used by various authorities, organisations and authors differ. Presently, there are no comprehensive statutory definitions of virtual currencies, cryptocurrencies and crypto assets that are accepted by all institutions and organisations in South Africa.

Before delving into technical aspects and definitions, it is worth noting the taxonomy of this innovation. The broad term used for this innovation is virtual currencies, which include all centralised and decentralised, convertible and non-convertible digital currencies.¹⁴ Cryptocurrencies fall within virtual currencies but are specifically decentralised and convertible virtual currencies (DCVCs) and crypto assets are the same as cryptocurrencies, but specifically named “assets” by authorities as it does not have legal tender status and it is currently mostly used for investment purposes.¹⁵

¹¹ <https://www.statista.com/statistics/647374/worldwide-blockchain-wallet-users/> (accessed: 25 May 2021).

¹² Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2020) 41-52.

¹³ Financial Action Task Force “Guidance for a Risk-Based Approach: Virtual Assets and Virtual Asset Service Providers” (2019) 6.

¹⁴ Financial Action Task Force FATF Report “Virtual Currencies - Key Definitions and Potential AML/CFT Risks” (2014) 4-6.

¹⁵ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2020) 8.

2.3.1 Virtual currencies, cryptocurrencies and crypto assets

The Financial Action Task Force (FATF) is an independent inter-governmental organisation that attempts to promote policies against terrorism financing and money laundering and consists of 37 jurisdictions and two regional organisation, with more than 200 countries committed to implement its recommendations and standards.¹⁶ This organisation, in its Report on Virtual Currencies, has comprehensively defined many terms used within the digital currency context, which definitions the South African Reserve Bank (SARB) have chosen to use in its Position Paper on Virtual Currencies as well.¹⁷

The FATF defines the term virtual currencies as a “digital representation of value” with the ability of being digitally traded.¹⁸ Furthermore, the FATF acknowledges that virtual currencies are a medium of exchange, a store of value and a unit of account, but that there is no legal tender status attached to cryptocurrencies as of yet.¹⁹ This entails that no person or institution is obliged to accept virtual currencies as payment for any product, service or debt.²⁰ Parties may however consent to virtual currency as payment, which gives it “currency” status in an *inter partes* sense. South Africa’s definitions and characteristics assigned to virtual currencies also indicate that it has no legal tender status and that these “currencies” are largely for investments purposes, which is why South African authorities have opted for the term crypto assets, for the time being.²¹

Apart from not possessing legal tender status, virtual currencies can be centralised, meaning that it can be issued by an authority such as the SARB, or it can be decentralised, which entails that there is no central governing authority issuing it.²² Virtual currencies can also be convertible, which means that it can be exchanged for real currency, or non-convertible, which entails it can only be used within the realm it was created for.²³

¹⁶ <http://www.fatf-gafi.org/about/whoweare/> (accessed: 18 May 2021).

¹⁷ South African Reserve Bank National Payment System Department “Position Paper on Virtual Currencies” (2014) 2.

¹⁸ Financial Action Task Force FATF Report: Virtual Currencies - Key Definitions and Potential AML/CFT Risks (2014) 4.

¹⁹ 4-5.

²⁰ 4.

²¹ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 15-16.

²² Financial Action Task Force FATF Report “Virtual Currencies - Key Definitions and Potential AML/CFT Risks” (2014) 5-6.

²³ 4-5.

The FATF distinguishes between virtual currencies and cryptocurrencies in the sense that cryptocurrencies are not only decentralised and convertible currencies, but are also protected by cryptography and requires public and private keys to perform transactions.²⁴ Cryptocurrencies specifically include the use of cryptography, which is what the blockchain technology is based on.²⁵ It also does not fall under electronic money as there is no centralised authority issuing it in any jurisdiction.²⁶ Cryptocurrencies are consequently a sub-group of virtual currencies and enjoy some of the characteristics the FATF ascribes to virtual currencies.

Given South Africa's acknowledgement of cryptocurrencies, which it prefers to refer to as crypto assets, it is no surprise that the Financial Sector Conduct Authority (FSCA) has suggested that crypto assets should be classified as a financial product in terms of the Financial Advisory and Intermediary Services (FAIS) Act 37 of 2002 in its draft Declaration.²⁷ This Declaration suggest that the statutory definition of crypto assets be

“... any digital representation of value that can be digitally traded, or transferred, and can be used for payment or investment purposes, but excluding digital representations of fiat currencies or securities that already fall within the definition of financial product”.²⁸

The significance of this declaration will be discussed in the next chapter, but when this declaration comes into effect, South Africa will have its first statutory definition of crypto assets.

Another important characteristic of cryptocurrencies is that they can operate across borders. No single jurisdiction can control the domain, which makes regulation even more problematic and creates various loopholes for users looking to commit various crimes.²⁹ This dissertation focuses largely on cryptocurrencies and crypto assets, due to the decentralised nature and the anonymity surrounding it, which is where many inherent risks and problems arise.

²⁴ 5-6.

²⁵ 5.

²⁶ 4.

²⁷ Financial Sector Conduct Authority “Draft Declaration of Crypto Assets as a Financial Product” (2020) 2.

²⁸ 2.

²⁹ Financial Action Task Force FATF Report “Virtual Currencies - Key Definitions and Potential AML/CFT Risks” (2014) 9-10.

2.3.2 Blockchain

Blockchain technology puts trust in mathematics instead of people in authoritarian positions.³⁰ The blockchain is the technology that allows cryptocurrencies to be decentralised as it makes use of a distributed public ledger, where every transaction ever executed is publicly recorded and available to all.³¹ It is universally accepted that the longest blockchain is the correct one.³²

It is worth noting that the blockchain technology can also be used for things such as smart contracts, whereby parties execute a contract, which is programmed using lines of code, when certain conditions are met.³³ The uses of blockchain technology in itself are even more complex and warrant extensive research as it becomes more prevalent in the future.

2.3.3 Mining

Mining refers to the process whereby cryptocurrencies are discovered.³⁴ Terms such as “created” and “generated” are incorrect as it implies that persons have control to make more of it, which is wholly untrue.³⁵ Mining accordingly puts cryptocurrencies into the system. Miners can thus sell these cryptocurrencies to exchanges, purchase goods and services or use them as an investment for themselves.³⁶

Mining is another part of decentralisation as it is not jurisdictionally bound, and no single person has control over any aspect of mining.³⁷ Miners are extremely difficult to regulate, and little has come forth in proposed regulations concerning miners.

³⁰ M Atzori “Blockchain technology and decentralised governance: Is the state still necessary?” (2017) 6 *Journal of Governance and Regulation* 1 45-62 46.

³¹ Financial Action Task Force “Guidance for a Risk-Based Approach: Virtual Assets and Virtual Asset Service Providers” (2019) 15.

³² D Erasmus & S Bowden “A Critical Analysis of South African Anti-Money Laundering Legislation with regard to Cryptocurrency” (2020) 41 *Obiter* 309-327 312.

³³ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 13.

³⁴ K Mitchell ‘Bitcoin from the Beginning’ (2014) 14 *Without Prejudice* 61-62 at 61.

³⁵ 62.

³⁶ Financial Action Task Force FATF Report “Virtual Currencies - Key Definitions and Potential AML/CFT Risks” (2014) 7.

³⁷ A Nieman “A Few South African Cents’ Worth on Bitcoin” (2015) 18 *PELJ* 1978-2010 1987.

2.3.4 Wallets and exchanges

Wallets are used by users to transact cryptocurrencies between each other. Wallet providers allow users to store cryptocurrencies, maintain the balance of cryptocurrencies and transact securely.³⁸

Wallets are similar to our commercial banks and make use of private and public keys of each user.³⁹ The public key is known by other parties, and it is the destination address of the user's wallet, which is akin to a bank account number.⁴⁰ A private key is akin to a PIN of a bank account. The user is the only one who knows the private key and it is necessary to execute the transaction.⁴¹ Both these keys are cryptographically encoded.⁴² The wallet provider has an online wallet (like an account), and the user has a wallet which is downloaded onto a smart device (like a banking app).⁴³ This area may be easier to regulate as wallet providers are to be considered accountable institutions in terms of the Financial Intelligence Centre Act 38 of 2001 (FICA).⁴⁴

Cryptocurrency exchanges are similar to foreign exchanges. These exchanges are the direct link between the cryptocurrency realm and the real economy as they allow users to access a trading platform, integrate wallets and convert real currency to cryptocurrency. Some popular South African exchanges include Luno, Altcointrader and Ice3x (pronounced "Icecubed", which is to be liquidated).⁴⁵

Wallets and exchanges are some of the most vulnerable places in the cryptocurrency sphere, especially for users, and are most likely to be regulated first as witnessed in the next chapter.

³⁸ Financial Action Task Force FATF Report "Virtual Currencies - Key Definitions and Potential AML/CFT Risks" (2014) 8.

³⁹ 5.

⁴⁰ L Sadhaseevan *The Regulation of Cryptocurrencies in the Context of South Africa's Financial Sector* (2019) LLM dissertation University of Kwa-Zulu Natal 27.

⁴¹ 28.

⁴² Financial Action Task Force FATF Report "Virtual Currencies - Key Definitions and Potential AML/CFT Risks" (2014) 5.

⁴³ L Sadhaseevan *The Regulation of Cryptocurrencies in the Context of South Africa's Financial Sector* (2019) LLM dissertation University of Kwa-Zulu Natal 2

⁴⁴ Financial Sector Conduct Authority "Draft Declaration of Crypto Assets as a Financial Product" (2020).

⁴⁵ <https://www.moneyweb.co.za/moneyweb-crypto/crypto-exchange-ice3-to-be-liquidated-suspends-all-withdrawals/> (accessed: 1 May 2021).

2.4 Operation of cryptocurrencies

The operation of cryptocurrencies is best explained by using an example of how transactions occur.

Where a transaction is executed between parties, it starts off with A obtaining cryptocurrency. This is done by downloading cryptocurrency software and then obtaining cryptocurrency through mining, exchanging real currency and/or purchasing cryptocurrencies from a Cryptocurrency Automated Teller Machine (CATM), such as the machine in Northwold Spar in Johannesburg.⁴⁶

A now has cryptocurrencies, which A must store. Storing can be done in a virtual wallet, using the private and public key. A, the payer, sends a payment request instruction, with the private key. B, the receiver, verifies this instruction by using A's public key. The next step is where mining occurs, whereby computing power is used to solve a set of complex mathematical problems, using algorithms, in order to verify the transaction.⁴⁷ This process constitutes a new block on the blockchain, and the payment is then confirmed, and the cryptocurrency is transacted. The blockchain has been extended with another block, which is a public record for all users to see. Users are allowed to be anonymous as no identification documentation is needed in order to transact and exchange cryptocurrencies.⁴⁸ This seemingly simple process already has many areas where regulatory intervention may be necessary.

2.5 Conclusion

A patchwork of definitions for virtual currencies, cryptocurrencies and crypto assets has come into existence over the last decade. Given the complexity of this technology, the definitions might change in future years as the uses change and expand. It is clear that with the high degree of anonymity, decentralisation and cross-border operation, regulatory intervention is necessary to protect users and potentially the economy as well.

⁴⁶ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 10.

⁴⁷ D Erasmus & S Bowden "A Critical Analysis of South African Anti-Money Laundering Legislation with regard to Cryptocurrency" (2020) 41 *Obiter* 309-327 311.

⁴⁸ Financial Action Task Force FATF Report "Virtual Currencies - Key Definitions and Potential AML/CFT Risks" (2014) 6.

Chapter 3:

The current regulatory landscape of cryptocurrencies in South Africa

3.1 Introduction

This chapter focuses on the current regulations in effect and those regulations being considered by various South African institutions and organisations. There are very little regulations surrounding virtual currencies in effect and new regulations are constantly being considered as regulators are still in the process of discovering the impact virtual currencies have across several legal and economic fields. The extent of these impacts will only be fully discovered once the use of virtual currencies become commonplace.

South Africa follows a risk-based approach when it comes to regulating crypto assets, attempting to find a balance between mitigating risks and encouraging innovation.⁴⁹ Many institutions have issued papers, recommendations, alerts and reports, which will be discussed in this chapter.

3.2 The National Treasury

The National Treasury together with the SARB, the South African Revenue Service (SARS), the Financial Services Board (FSB) and the Financial Intelligence Centre (FIC) issued a user alert in 2014 to all virtual currency users, advising “extreme caution”, as the unregulated status makes it incredibly precarious and affords little to no recourse if anything adverse occurs.⁵⁰

As South Africa’s principal department to manage economic policy and finances, the regulation of cryptocurrencies is of great concern to the National Treasury. Save for the 2014 alert, the National Treasury has also proposed that Item 19 of Schedule 1 of FICA be amended to include under accountable institutions:

“A person who carries on the business of one or more of the following activities or operations for or on behalf of a client:

- a) exchanging a crypto asset for a fiat currency or vice versa;

⁴⁹ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2020) 22.

⁵⁰ National Treasury “User Alert Monitoring of Virtual Currencies” (2014) 1-4.

- b) exchanging one form of crypto asset for another;
- c) conducting a transaction that moves a crypto asset from one crypto asset address or account to another;
- d) safekeeping or administration of a crypto asset or an instrument enabling control over a crypto asset, and
- e) participation in and provision of financial services related to an issuer's offer or sale of a crypto asset."

This entails that all crypto asset service providers (CASPs) such as wallets, exchange platforms, traders trading on behalf of a client and advisers must adhere to the relevant provisions of the Act. This recommendation is in line with international best practices that South Africa adheres to as member of the FATF.

The significance hereof is that these parties will have a duty to identify their clients, keep records of any relevant information (such as transactions, identities and accounts) and have to keep proper records of the clients.⁵¹ These parties will also have reporting duties, which means that they will have to provide the FIC with the details of their clients where the Centre requests same and the Centre may intervene in transactions it deems suspicious.⁵² Where these parties do not comply with the Act, they will be committing an offence, which gives this piece of legislation the necessary teeth it needs in order to protect users and to combat crimes such as money laundering and the financing of terrorism.⁵³

By amending this piece of legislation, the substantial issue of anonymity will be addressed as a proper identification document must be required and stored. It is worth noting though that the practicality of this may be an issue, as it is easy for South African users to use a wallet or exchange in another country where these regulations do not exist.

3.3 The South African Reserve Bank

The most notable action the SARB has taken was to issue its Position Paper on Virtual Currencies in 2014.⁵⁴ This Paper is not legally binding and merely contains policy approaches and it discusses whether or not cryptocurrency is a legal tender and/or

⁵¹ SS 23-25 of FICA.

⁵² S 29 and S 34 of FICA.

⁵³ Ch 4 of FICA.

⁵⁴ South African Reserve Bank "Position Paper on Virtual Currencies" (2014).

electronic money, the potential risks associated with cryptocurrencies and the regulatory position, but has no practical effect.⁵⁵

It contends that cryptocurrencies are neither electronic money nor legal tender and substantiates this position by referring to the definition of legal tender in section 14 of the South African Reserve Bank Act 90 of 1989.⁵⁶ The SARB classified the risk elements with regard to payment systems and payment service providers, price stability, anti-money laundering and combating terrorist financing (AML/CFT), consumer risks, circumvention of exchange control regulations and financial stability.⁵⁷ The SARB aptly acknowledges that cryptocurrencies are unregulated and furthermore that the entire risk is on the end-user's shoulders as the SARB does not regulate, oversee or supervise virtual currencies.⁵⁸ The unregulated environment exacerbates the risks attached to using cryptocurrency and serious intervention needs to occur in order to mitigate the risks.

The current stance is that the SARB is monitoring the environment, but no implemented regulations have transpired since the issuing of this Paper, that there is no significant risk to price and financial stability or the National Payment System as yet, while the SARB also encourages innovation.⁵⁹

3.4 The South African Revenue Services

The South African Revenue Service (SARS) is a large stakeholder where cryptocurrencies are concerned, as it provides many opportunities for income to be generated, which can in turn be taxed. SARS uses the term "cryptocurrencies", but the IFWG has suggested that it adopts a uniform definition using the term "crypto assets" instead.⁶⁰ In its April 2018 media release, SARS provided that earnings from cryptocurrency trading and investing are subject to income tax and capital gains tax in South Africa.⁶¹ The onus is on users to disclose their cryptocurrency earnings.⁶² This

⁵⁵ D Erasmus & S Bowden "A Critical Analysis of South African Anti-Money Laundering Legislation with regard to Cryptocurrency" (2020) 41 *Obiter* 309-327 317.

⁵⁶ South African Reserve Bank "Position Paper on Virtual Currencies" (2014) 4-5.

⁵⁷ 6-12.

⁵⁸ 12.

⁵⁹ 12-13.

⁶⁰ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 27.

⁶¹ South African Revenue Services Media Release "SARS'S Stance on the Tax Treatment of Cryptocurrencies" (2018) 1-2.

⁶² 1-2.

can however easily be circumvented, given the anonymity currently allowed within exchange platforms and wallets and the fact that cryptocurrencies do not operate within borders.

SARS has explained that cryptocurrency is an intangible asset and not real currency and proposed that it be treated as a financial instrument.⁶³ As of 1 April 2019, cryptocurrencies are included in the definition of financial instruments under section 1 of the Income Tax Act 58 of 1962. Where income tax is considered, the definition of “gross income” as per section 1 of the Act must be considered. The core elements of the definition are an amount in cash or otherwise; received by or accrued to a resident; excluding receipts or accruals of a capital nature.⁶⁴ Although cryptocurrencies cannot constitute cash, due to the absence of legal tender status, it can be valued in Rand terms in order to ascertain what amount was received or accrued as envisaged in the definition of “gross income”.⁶⁵ Accordingly, normal income tax rules apply for revenue from cryptocurrency transactions. In order to determine if the accrual is income or capital in nature, it is tested in accordance with existing jurisprudence.⁶⁶

Where Value-Added Tax (VAT) is considered, the amendment of “financial services” in section 2 of the Taxation Laws Amendment Act 23 of 2018, which came into effect on 1 April 2019, saw to the inclusion of cryptocurrencies. This includes

“the issue, acquisition, collection, buying or selling or transfer of ownership of any cryptocurrency:

Provided that the activities contemplated in paragraphs...(o) shall not be deemed to be financial services to the extent that the consideration payable in respect thereof is any fee, commission, merchant’s discount or similar charge, excluding any discount cost.”⁶⁷

Therefore, cryptocurrency dealings are generally exempt from VAT in terms of section 12 of the Value Added Tax 89 of 1991. The IFWG has mentioned that VAT leakage may occur with increased use of cryptocurrencies, especially in the use case of payments using cryptocurrencies.⁶⁸ Thus, we might see a change with this tax aspect.

⁶³ 1.

⁶⁴ Section 1 of the Income Tax Act 58 of 1962.

⁶⁵ Select Committee on Finance “A guide to understanding cryptocurrency issues and regulatory frameworks” (2021) Parliamentary Budget Office 31.

⁶⁶ 31.

⁶⁷ Tax Law Amendment Act 23 of 2018.

⁶⁸ National Treasury and SARS “Draft Response Document on Taxation Laws Amendment Bill, 2018 and Tax Administration Laws Amendment Bill, 2018” (2018) 34.

There is however little said around how miners should be taxed and there will presumably be new suggestions on this soon. Clearly, the regulation of cryptocurrencies insofar tax is concerned is already in motion and will evolve as the landscape changes.

3.5 Other organisations and institutions

3.5.1 Financial Sector Conduct Authority

The Financial Sector Conduct Authority (FSCA), which replaced the FSB, has come up with an interim solution until the Conduct of Financial Institutions (COFI) Bill comes into effect and the Financial Sector Regulation Act 9 of 2017 (FSRA) is amended. This solution entails expanding the definition of “financial product” to include crypto assets, as explained in its draft Declaration.⁶⁹

The FSCA has the power to designate any additional products as a financial product by making a declaration.⁷⁰ The implication of this is that all the persons that fall under the definition of a financial service provider under the FAIS Act, in other words CASPs, will have to be registered as same and adhere to the provisions thereof.⁷¹ This will ensure that users will have some form of recourse against non-compliant CASPs and that users will enjoy more protection when making use of CASPs.⁷²

3.5.2 Intergovernmental Fintech Working Group’s Crypto Asset Regulatory Working Group

The Intergovernmental Fintech Working Group’s Crypto Assets Regulatory Working Group (IFWG) consists of the National Treasury, SARS, SARB, FSCA, FIC, Competition Commission and National Credit Regulator.⁷³ The latter two members were added in the 2021, showing that the IFWG attempts to address regulation as comprehensively as possible.

⁶⁹ Financial Sector Conduct Authority “Draft Declaration of Crypto Assets as a Financial Product” (2021) 1.

⁷⁰ Financial Sector Conduct Authority “Statement in Support of the Draft Declaration of Crypto Assets as a Financial Product under the Financial Advisory and Intermediary Services Act” (2020) 2.

⁷¹ 4.

⁷² 2.

⁷³ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 1.

The Group's approach has been to identify what the uses of cryptocurrencies are, which have resulted in five use cases.⁷⁴ These use cases are identified as buying and selling, using cryptocurrencies as a medium of exchange, ICOs, crypto asset funds and CASPs. From these use cases, the IFWG has identified risks emanating from the uses, which risks can be generic or specific and are discussed in Chapter 4.⁷⁵

Based on these risks, the IFWG proposes regulations with due regard given to the risk-based, unified and phased approaches.⁷⁶ The overall recommendations include that all crypto asset service providers should be regarded as CASPs and that FICA be amended to include CASPs as accountable institutions, as mentioned above.⁷⁷ As such, the FIC is recommended to have a supervisory role over CASPs to ensure their compliance.⁷⁸ The IFWG must also design a crypto asset monitoring programme, which would include transaction volumes, number of merchants and retailers accepting crypto assets as payment, cross-border flows, volumes of crypto assets bought at vending machines and overall market capitalisation of crypto assets.⁷⁹ Furthermore, it has been recommended that no legal tender status should be awarded, crypto assets should not be allowed for the conduct of money settlements, the Prudential Authority must consider appropriate responses and that institutions use a unified term and definition for crypto assets.⁸⁰

There are specific recommendations made for each use case as well and these recommendations will be discussed in Chapter 7. Clearly, an immense amount of work has been put into these recommendations and they should be introduced and included where necessary and appropriate.

3.6 Conclusion

Although many regulations have been proposed and pondered, very few of these regulations are in full force and effect and presently the virtual currency landscape

⁷⁴ 14.

⁷⁵ 22-27.

⁷⁶ 29-30.

⁷⁷ 30-35.

⁷⁸ 34.

⁷⁹ 34.

⁸⁰ 35.

remains largely unregulated. However, this will undoubtedly change in the years to come, given the increasing use of virtual currencies and specifically cryptocurrencies.

South Africa's approach has been largely reactive, and it seems to be a good balanced approach, which encourages innovation that can lead to economic growth, while mitigating risks as they arise. All relevant authorities have done research on virtual currencies and issued a report, alert, position paper or the like so as to give users some clarification. It must be said, however, that there is a lot more that will have to be done for full integration and before the comfortable use of cryptocurrencies is possible.

Chapter 4:

Inherent problems and risks of cryptocurrency

4.1 Introduction

Cryptocurrency poses unique risks and problems due to its inherent anonymous and unregulated nature, combined with its novelty which includes volatility. The IFWG has classified risks as general or specific and has comprehensively elaborated on the identified risks.⁸¹ Legal intervention has to be implemented for consumer protection, and the current and potential growth of cryptocurrencies highlights the need for further future regulation in order to protect the integrity of the economy. This chapter outlines the inherent risks and problems described by the IFWG, which must be addressed if seamless integration between cryptocurrency and the national payment system is to be achieved.

4.2 General risks

The IFWG has outlined certain general risks pertaining to cryptocurrency. These risks can be viewed as broad risks that should be considered over the long term, and which have the inherent capability to change the way business is conducted and economies operate.

The first generic risk is the development of a parallel, fragmented and non-sovereign monetary system created by cryptocurrencies.⁸² This in essence entails that the SARB will be completely undermined if large percentages of citizens use only or mostly cryptocurrencies and no fiat currencies. This in turn will entail that the ability to use monetary policy to stabilise output and influence prices will be futile, leaving us with a free market economy.⁸³ The IFWG is of the opinion that this is the risk with the widest-ranging implication as it threatens the existing financial system.⁸⁴ The implications may be far-reaching where an alternative financial system exists as no government intervention (such as adjusting interest rates) can be used to “correct”

⁸¹ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 22-27.

⁸² 22.

⁸³ 22.

⁸⁴ 22.

equilibrium prices and outputs. This systemic risk is however not currently being addressed as it is nowhere near to materialising.

The second risk concerns consumer protection, market efficiency and market integrity risks.⁸⁵ These risks are more pressing as they are already present. The lack of consumer protection is glaring, which is clear from the recent Africrypt scam.⁸⁶ Twin brothers made off with 3.6 billion dollars, the largest cryptocurrency scam to date, by attempting to make their clients believe they were hacked.⁸⁷ However, the FSCA cannot launch a formal investigation, since cryptocurrencies are not yet financial products, thereby limiting the victims' right of recourse. Another example would be the recent developments on the Binance trading platform. Binance, which is a lesser known platform in South Africa that has been subject to insider trading scandals, is terminating certain services in South Africa.⁸⁸ This comes after the FSCA intervened for the sake of consumer protection as Binance was given financial advice and providing intermediary services.⁸⁹ This example shows how easy it has been thus far for any person to render intermediary services and give financial advice, which can place many consumers in particularly vulnerable spots, especially given the lack of recourse.

Further concerns are market efficiency and integrity, increased money laundering and terrorist financing, circumvention of exchange control, increase in undetected and illegitimate cross-border financial flows, inaccurate balance of payments data, illegitimate purchases and tax evasion.⁹⁰ These concerns and risks are related to the anonymity aspect of cryptocurrency. If no comprehensive record is kept of users by intermediaries such as wallet providers, then there is no way to track users or parties to transactions. The only way to address these concerns emanating from anonymity is through intermediaries, since the blockchain technology itself will not allow for transparency in this regard.

⁸⁵ 22.

⁸⁶ <https://www.bloomberg.com/news/articles/2021-06-23/s-african-brothers-vanish-and-so-does-3-6-billion-in-bitcoin> (accessed: 26 June 2021).

⁸⁷ <https://www.bloomberg.com/news/articles/2021-06-23/s-african-brothers-vanish-and-so-does-3-6-billion-in-bitcoin> (accessed: 26 June 2021).

⁸⁸ <https://news.bitcoin.com/crypto-exchange-binance-terminates-some-services-south-africa-warning-by-regulator/> (accessed: 22 October 2021).

⁸⁹ <https://news.bitcoin.com/crypto-exchange-binance-terminates-some-services-south-africa-warning-by-regulator/> (accessed: 22 October 2021).

⁹⁰ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2021) 22.

The third risk identified by the IFWG is the existence of an undefined and incomplete legal and regulatory framework which does not provide solutions for potential cryptocurrency associated risks.⁹¹ The IFWG's objective assessment maintains that its members may not identify or mitigate every risk. Furthermore, it cannot gain a holistic view and respond appropriately if it does not have accurate information on the flow and volume of cryptocurrencies in South Africa, or the monetary equivalent in Rand.⁹² Again, this risk is based on the fact that there is a great deal of missing information due to the anonymity and lack of reporting when dealing with cryptocurrencies – authorities cannot gain a 360-degree view if they are blocked by an inherent characteristic of this innovation, which has not been addressed thus far.

These individual risks are inter-related and if viewed as a unit, it becomes clear why there was a need to establish a group such as the IFWG to address these potentially severe risks. The IFWG's most important responsibility is to keep monitoring the generic risks and respond with swiftly implemented regulations.

4.3 Specific risks

Whilst keeping the generic risks in mind, the IFWG went further to outline specific risks based on each of the five use cases identified.

4.3.1 Use case 1: Buying and/or selling crypto assets by individual consumers and legal persons

The IFWG has identified five risks emanating from this use case. The first risk is money laundering and terrorist financing.⁹³ To that end implementing AML/CFT measures must be prioritised. The inherent problems with these measures are the anonymity aspect and the cross-border operation nature of cryptocurrencies. There are currently no operational regulations that will decrease anonymity in purchasing, trading or converting cryptocurrency through CASPs. The anonymity is a twofold problem as customers cannot be identified and even if they can be identified, no transactions can

⁹¹ 22.

⁹² 22.

⁹³ 23-24.

be traced to them – leaving little recourse where crimes occur, as was seen with Africrypt.

Some CASPs are voluntarily implementing measures to identify and verify customers, but no measures are currently legally binding.⁹⁴ The only obligation on CASPs is to report suspicious and unusual transactions in accordance with FICA.⁹⁵ The question must be asked if CASPs will indeed be able or willing to report suspicious transactions given that no identification and verification obligations exist. The FIC might well be kept in the dark about any of these dubious customers and transactions. The only way to implement AML/CFT measures is to target CASPs and require customer due diligence.

The second risk concerns exchange controls, where the absence of regulations makes it easy to circumvent exchange control regulations, such as reporting requirements.⁹⁶ It is not currently possible to track the movement of money through cryptocurrencies and therefore exchange control regulations cannot be monitored and are essentially easily circumvented. The IFWG speaks to the transparency of the financial system that is lost – which is a fundamental feature of the distributed ledger system.⁹⁷ Even if CASPs are regulated, it cannot be said that this characteristic can be countered, since there will always be less transparency in cryptocurrency payment systems compared to that of the current payment systems.

Where CASPs sell cryptocurrencies, they may elect to purchase from international providers, increasing liquidity in the South African market.⁹⁸ However, the Currency and Exchanges Manual for Authorised Dealers does not allow cross-border or foreign currency transfer where the intention is to purchase cryptocurrency as it is not recognised legal tender in South Africa, nor has it been allocated to an asset class.⁹⁹ Thus, CASPs look for alternative ways to buy cryptocurrency and these measures are not necessarily compliant with regulations and leaves authorities with incomplete information.

⁹⁴ 23.

⁹⁵ Section 29 of FICA.

⁹⁶ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 23.

⁹⁷ 23.

⁹⁸ 23.

⁹⁹ 23.

Thirdly, market conduct risk is identified. CASPs are unregulated which leaves consumers vulnerable to fraud and unable to resolve disputes appropriately.¹⁰⁰ Due to the novelty, many people can be taken advantage of, especially given the lack of cryptocurrency information shared with unschooled citizens. CASPs may also charge exorbitant fees and hidden charges, with no watchdog to hold them accountable.

The next risk involves advice and mis-selling risks.¹⁰¹ It is trite that there are many risks when transacting or investing in cryptocurrency, but the general trend is that only the positive aspects are highlighted. This increases the chances that customers will conduct or receive inappropriate risk-analyses, needs and suitability assessments which may potentially result in massive losses, especially for uninformed and vulnerable users.¹⁰²

Lastly, there is an operational risk involving cybersecurity risks.¹⁰³ Cryptocurrency revolves around cybertechnology, which means it is exposed to cybercrime. Various hacks and cyber-attacks for ransom on platforms have been performed, resulting in incredible losses. The only way these hacks can be combatted are through “counter-hacks”, which are also illegal. Cybercrime is comprehensively dealt with in the next chapter, since it is one of the areas of law most influenced by cryptocurrency.

4.3.2 Use case 2: Payments using crypto assets

The generic risk of a parallel, unregulated and fragmented payment system is again mentioned as a risk – a prime example that risks are inter-related.¹⁰⁴ As previously discussed, the central bank will have no role in this “new payment system”, since it makes use of distributed ledger technology independent from a central regulating authority. This risk goes hand-in-hand with the risk of an inefficient payment system. Practically the alternative cryptocurrency payment system will not only circumvent the central authority but commercial banks as well, which will have an enormous impact on the struggling labour market.

¹⁰⁰ 23-24.

¹⁰¹ 24.

¹⁰² 24.

¹⁰³ 24.

¹⁰⁴ 24.

The risk of perceived regulatory acceptance is also concerning.¹⁰⁵ This ties in with the lack of cryptocurrency information given to users. Lastly, operational risk and a lack of consumer protection for crypto asset payments again arise, since there is no way for payments to be reversed at this stage and no recourse may exist where overpayments, fraudulent or erroneous payments have been made.¹⁰⁶ It is noteworthy that this ties in with anonymity and tracing issues. Furthermore, consumer protection is an issue due to the lack of knowledge together with volatility of all types of cryptocurrencies.

4.3.3 Use case 3: Capital raising through ICOs

The risks associated with ICOs have largely been covered by the first two use cases, such as AML/CFT measures, unclear legal frameworks and cybersecurity risks such as fraud.¹⁰⁷ To combat these risks, the FATF proposed that anyone who provides financial services relating to the issuance of coins should be obliged entities, which are obliged to implement and adhere to AML/CFT measures as imposed.¹⁰⁸

Other risks include the high risk of failure and the concomitant risk to investors.¹⁰⁹ ICOs are mostly issued by start-up companies, which are notorious for failing. These businesses do not necessarily have the framework in place to reimburse investors, should they fail. Even if they do not fail, the return on investment might be unfavourable in any event.¹¹⁰ There is no doubt that major risks are present when investing in ICOs. Connected to this risk is the risk of incomplete and/or inaccurate disclosure of the business plan and its operation.¹¹¹ This makes it easy to commit fraud as well, further increasing risk. Thus, ICOs are highly speculative and where investors want to exit, there might be no such opportunity due to the absence of regulations or the inability to convert the coin to fiat currency.¹¹² Lastly, the fiscal framework may be lacking in terms of tax regulations due to the nascent nature of cryptocurrencies.¹¹³

¹⁰⁵ 25.

¹⁰⁶ 25.

¹⁰⁷ 25-26.

¹⁰⁸ Financial Action Task Force FATF Report “Virtual Assets and Virtual Asset Service Providers” (2019) 48.

¹⁰⁹ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 26.

¹¹⁰ 26.

¹¹¹ 26.

¹¹² 26.

¹¹³ 26.

4.3.4 Use case 4: Crypto asset funds and derivatives

This use case is susceptible to the risks of an undefined legal framework and volatility – mentioned in duplicate by the IFWG and already addressed herein.¹¹⁴ Furthermore, the Group mentions unsystematic risk, which emanate from the difficulty to manage cryptocurrency investment funds as investment returns, seeing as the market is haphazard and uncorrelated to general market risk.¹¹⁵ The difficulty in setting risk levels transpire as modelling risk exposure is problematic due to the absence of historical data and the fact that it is subject to unclear liquidity assumptions.¹¹⁶ Consequently, determining the risk level is near impossible. Uncorrelated price movements also contribute to these risks as the general market trends are irrelevant and it is often difficult to determine direction and size of fluctuations.¹¹⁷ This behaviour also shows how unsystematic cryptocurrencies can be.

Linked to these risks is liquidity risk, which should be considered as there is a concentration of ownership, low levels of trading and difficulty to convert to liquid assets, according to the IFWG. Trading levels are increasing daily however, with more than two million users in South Africa during 2020.¹¹⁸ Wallets make it convenient to convert cryptocurrency to fiat currency, and the risk here lie more with the volatility, as a user may have substantial losses if an event necessitates the immediate conversion of cryptocurrency to fiat. Investing in cryptocurrency at this stage is patently complex and exceptionally risky. These risks might become insignificant if there is increased transparency and if fluctuations are less radical.

An example of such extreme volatility occurred on 21 October 2021, where Bitcoin plummeted from sixty five thousand US dollars to eight thousand US dollars, but only on the Binance US trading platform, whereas on other platforms the lowest point was only sixty four thousand dollars.¹¹⁹ The variance on different platforms

¹¹⁴ 27.

¹¹⁵ 27.

¹¹⁶ 27.

¹¹⁷ 27.

¹¹⁸ <https://businesstech.co.za/news/banking/495569/the-real-number-of-people-investing-in-bitcoin-and-other-cryptos-in-south-africa-treasury/> (accessed: 15 June 2021).

¹¹⁹ <https://markets.businessinsider.com/news/currencies/bitcoin-price-crashed-87-percent-8200-binance-us-crypto-platform-2021-10> (accessed: 21 October 2021).

contains incredible risks to consumers and is largely due to the fact that there are no standardised way to value cryptocurrency and set the price thereof.¹²⁰

4.3.5 Use case 5: Crypto assets market support

There are two different risks concerning this use case namely, cybersecurity and environmental risks.¹²¹

Cybersecurity is an exceptionally big risk, which is an aspect present in most other risks mentioned in this chapter as well. The nature of cryptocurrency provides an ideal environment for cybercrime to flourish. This is exacerbated by the fact that South African crime prevention authorities are ill-equipped to deal with cybercrimes, with very few law enforcement officers trained in how to deal with a situation where, for example, a hack occurs – making a country like South Africa a prime target for opportunistic cybercriminals.¹²²

Environmental risks arise where cryptocurrency mining takes place.¹²³ Mining requires an immense amount of electricity, which results in an increase in pollution. There should be an alternative plan in place to ensure that mining does not contribute to climate change, and some countries have created initiatives involving the use of volcanoes.¹²⁴

4.4 Conclusion

These risks are by no measure a closed list – there are numerous other risks that have not been identified yet, which will only appear as the use of cryptocurrencies increase. The risks discussed are those currently identified and most apparent and/or systemic to such an extent that they should already be kept in the back of the mind of regulators.

¹²⁰ <https://markets.businessinsider.com/news/currencies/bitcoin-price-crashed-87-percent-8200-binance-us-crypto-platform-2021-10> (accessed: 21 October 2021).

¹²¹ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 27.

¹²² S Dlamini & C Mbambo “Understanding policing of cyber-crime in South Africa: The phenomena, challenges and effective responses” (2019) *Cogent Social Sciences* 6-7.

¹²³ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 27.

¹²⁴ <https://www.npr.org/2021/06/11/1005231250/el-salvador-plans-to-use-electricity-generated-from-volcanoes-to-mine-bitcoin> (accessed: 15 July 2021).

The IFWG has comprehensively discussed the most important risks and the way these risks are monitored and addressed in future will largely determine the success of economic integration of cryptocurrency and reaping the benefits thereof.

Chapter 5:

Influences and risks of cryptocurrency in specific areas of law

5.1 Introduction

The foundation of the risks has been laid out in the previous chapter. This chapter builds thereon by briefly analysing the influences and risks pertaining to specific areas of law. With the increased use and popularity of cryptocurrencies, certain areas of law will feel major impacts and completely new legal questions will arise from transacting with and investing in cryptocurrency.

5.2 Contract law

Contract law is arguably the area of law currently most influenced by cryptocurrency. Globally cryptocurrency is being treated as property and smart contracts are becoming legally enforceable.¹²⁵

Smart contracts are complex, but essentially require that the conditions of the contract are written into the blockchain and once all the conditions are fulfilled, the contract is executed and payment occurs.¹²⁶ The irreversible nature of cryptocurrency transactions poses issues, especially regarding agency. Where the principle or agent commits fraud or where payment is made to the wrong party (which may occur if the public key is entered incorrectly) there is no way to reverse the transaction.¹²⁷ The anonymity of cryptocurrencies may also pose an issue in cases such as where capacity or authority are questioned, which may only be addressed once CASPs are required to do their customer due diligence.

There is also a lack of remedies available for parties to a contract who are defrauded, for example the Africrypt scam.¹²⁸ Cryptocurrencies are not currently in the

¹²⁵ R Schwinger "Blockchain law property and contract in the digital world" (2020) *New York Law Journal* 1.

¹²⁶ <https://searchcompliance.techtarget.com/definition/smart-contract> (accessed: 2 August 2021).

¹²⁷ <https://www.hfw.com/How-are-contract-and-trust-law-principles-applied-in-cryptocurrency-disputes-July-19> (accessed: 2 August 2021).

¹²⁸ <https://www.bloomberg.com/news/articles/2021-06-23/s-african-brothers-vanish-and-so-does-3-6-billion-in-bitcoin> (accessed: 26 June 2021).

regulatory remit to an extent where authorities are allowed to intervene in scams like this. Legal intervention is currently too limited and where vulnerable persons are taken advantage of and contracts are entered into, they are left without any protection.

Deeds are also worth mentioning, since it is legally possible to purchase immovable property with cryptocurrency. The transactions must be done in “cash”, as it is not possible to obtain a mortgage bond with cryptocurrency, given the decentralised nature and the absence of something akin to commercial banks.¹²⁹ Furthermore, guarantees against the funds cannot be delivered, as CASPs are not financial institutions, and this makes the transactions substantially riskier.¹³⁰ Lastly, if a deposit was paid and the offer to purchase is cancelled, the buyer may not be repaid, since cryptocurrency transactions are irreversible.

There are numerous aspects, such as the *essentialia* and *naturalia*, of contract law which are bound to be influenced by cryptocurrency in the near and far future. These aspects will undoubtedly lead to new legal questions from case law, and it will be interesting to see how the courts deal with these disputes.

5.3 Banking law

Cryptocurrency will influence both central banks and commercial banks in many different ways. Neither central nor commercial banks are currently under threat from cryptocurrencies, but it is worth discussing due to the far-reaching implications future threats may have.

Commercial banks have asked questions such as: “Will cryptocurrency be the reason for the end of paper currency?”¹³¹ If cryptocurrencies become widely used and accepted, commercial banks will be completely circumvented if they do not incorporate cryptocurrency, especially if cryptocurrencies enjoy price stability.¹³² CASPs, such as wallet providers, may even become a new type of “bank” in the case of price stability. This is however a long way off, as Visa for example handled more than 100 times the number of transactions compared to Bitcoin in 2018.¹³³ Commercial banks should thus

¹²⁹ <https://pmg.org.za/committee-meeting/33029/> (accessed: 29 July 2021).

¹³⁰ <https://pmg.org.za/committee-meeting/33029/> (accessed: 29 July 2021).

¹³¹ <https://www.brookings.edu/blog/up-front/2018/05/21/digital-currencies-five-big-implications-for-central-banks/> (accessed: 30 July 2021)

¹³² <https://www.brookings.edu/blog/up-front/2018/05/21/digital-currencies-five-big-implications-for-central-banks/> (accessed: 30 July 2021).

¹³³ <https://www.brookings.edu/blog/up-front/2018/05/21/digital-currencies-five-big-implications-for-central-banks/> (accessed: 30 July 2021).

be aware of these possibilities and monitor the situation continuously. In the event that these risks become realities, banks should already have the proper strategy in place to incorporate cryptocurrencies in order to stay relevant.

Central banks, on the other hand, sit with the systemic risk that the national payment system is rendered void by cryptocurrencies.¹³⁴ Central banks have also been advised, where this risk becomes pressing, to create their own virtual currency and to further regulate cryptocurrencies in order for the national payment system to stay intact.¹³⁵

Banking law will only see risks from cryptocurrency if there it is widely accepted and used across the country. The risks are of such a nature that they should be monitored constantly and the true volume of cryptocurrencies has to be determined in order for the response to be timely and appropriate.

5.4 Tax law

Tax law has already been touched on in previous chapters. The issues with tax law are the self-reporting responsibilities coupled with anonymity aspects, making it a recipe for disaster, while the cross-border nature adds even more issues.

Currently, underreporting of cryptocurrency related income is a considerable problem, which authorities ascribe to dishonesty and a lack of prescribed regulatory environments.¹³⁶ In order to combat tax evasion, the anonymity aspects must be addressed, as the IFWG is intent on doing, but the cross-border nature and flows may be more difficult to regulate successfully. Foreign persons can very easily use South Africa for tax evasion, as they might not be subject to every regulation imposed by South African authorities. The IFWG needs to address how it will monitor cross-border flows and how it will ensure that the parties to the transactions are not *mala fide*, especially where those parties are foreign. Lastly, as explained below, the practicality of investigation where tax evasion is present poses a problem if the boots on the ground are unable to comprehend the intricate nature of blockchain, distributed ledger systems and cryptography.

¹³⁴ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 10.

¹³⁵ <https://www.brookings.edu/blog/up-front/2018/05/21/digital-currencies-five-big-implications-for-central-banks/> (accessed: 30 July 2021).

¹³⁶ Select Committee on Finance “A guide to understanding cryptocurrency issues and regulatory frameworks” (2021) Parliamentary Budget Office 11.

5.5 Cybercrime

Cybercrime is the type of crime that is ever-present when dealing with cryptocurrencies. The Cybercrime Act 19 of 2020 is the primary piece of legislation that will deal with crypto-crimes such as money laundering, hacking, fraud, investor scams and cyber extortion.¹³⁷ This is of particular concern in South Africa, as no matter how much we regulate cryptocurrencies and related activities, if the practical investigations cannot yield evidence, the burden of proof cannot be satisfied and no convictions can be made.

The provisions of the Cybercrimes Act can be used to effectively investigate and prosecute crimes where cryptocurrencies are involved.¹³⁸ The Act, however, does not cater for instances where online means are used for proceeds from illegal activity which may be laundered and, therefore, existing common and statutory law remedies must be relied on.¹³⁹ This limitation will have to be addressed if the existing remedies fail to protect victims of these crimes.

The other major issue with cybercrime is the practicality of the investigations. South Africa's law enforcement is unfortunately markedly illiterate when it comes to new technology. Due to the fact that cybercrime is quick to cover up and leaves little or no trace, we need speedy response with an exceptionally competent team to deal with incidents such as hacking and cyber-extortion.¹⁴⁰

Currently, South Africa is making good headway for suitable regulations to be constructed and implemented. Unfortunately, without competent task forces and investigators, the regulations will be rendered toothless by the time they are put to the test. The IFWG made no mention of how this practical aspect might be addressed and it is contended that the failure to address this issue will leave South Africa as a prime target for cryptocurrency related crimes.

5.6 Conclusion

This chapter illustrates what cryptocurrency can do to certain areas of law and the degree to which it can cause peril and confusion. There are numerous other avenues

¹³⁷ E Reddy "Analysing the Investigation and Prosecution of Cryptocurrency Crime as Provided for by the South African Cybercrimes Bill" (2019) 41 *Statute Law Review* 1-14 1.

¹³⁸ 14.

¹³⁹ 14.

¹⁴⁰ 13.

that will also be influenced by the acceptance of cryptocurrency into our everyday lives. Clearly, cryptocurrency has the ability to destabilise the regulatory landscape and promises to pose interesting new legal questions for practitioners in the future.

Chapter 6:

International perspectives and comparison of regulations

6.1 Introduction

Authorities worldwide are aiming at regulating cryptocurrencies, with each country implementing different regulations as per the concerns they prioritised. This chapter outlines a few different approaches that various countries have taken in an attempt to regulate cryptocurrencies. The extent of the regulations ranges from hostile to completely accepting.

It would be befitting for the South African regulatory authorities to study the different approaches, since it will provide valuable insight into regulatory aspects which South Africa may adopt and amend to fit our landscape. The IFWG conducted an international analysis in its 2020 paper but disregarded it in the 2021 updated paper.

6.2 Canada

Canada's approach is the approach most similar to South Africa's. The IFWG has assessed Canada's position towards cryptocurrencies as neutral – being neither hostile nor excessively welcoming towards the various uses of cryptocurrencies.¹⁴¹ The Bank of Canada, the Canadian central bank, has been monitoring cryptocurrencies within its borders.¹⁴² Canadian authorities seem to prefer using the term digital currency.

Various documents have also emanated from Canada's regulatory authorities, which provide that cryptocurrencies are seen as assets and securities, akin to stock trading – which is similar to South Africa's current stance.¹⁴³ Furthermore, like South Africa, Canada does not consider cryptocurrencies to be legal tender.¹⁴⁴ The Canadian government's website informs that cryptocurrencies may be used in cases

¹⁴¹ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 41 – 43.

¹⁴² 41-43.

¹⁴³ <https://www.canada.ca/en/financial-consumer-agency/services/payment/digital-currency.html> (accessed: 29 June 2021).

¹⁴⁴ <https://www.canada.ca/en/financial-consumer-agency/services/payment/digital-currency.html> (accessed: 29 June 2021.)

where service providers or suppliers accept it, acknowledging that it can be used as a kind of *inter partes* private tender.¹⁴⁵

The taxation of cryptocurrencies in Canada entails that where a seller sells goods and receives payment in cryptocurrencies, such payments must be reflected in the seller's income tax.¹⁴⁶ Good and Service Tax and Harmonised Tax apply to the fair market value of goods and services bought with cryptocurrency – bringing cryptocurrency into the regulatory ambit.¹⁴⁷ Here anonymity is not an issue, as an audit on any establishment's financial and stock records will display these transactions and it is the business as seller that has to pay the tax, not any anonymous buyer. Where cryptocurrency is bought and sold like a commodity, persons must report the gains and losses from the trading of cryptocurrencies in their taxes as cryptocurrencies are considered a commodity which is subject to barter rules as well as the provisions of the Income Tax Act R.S.C., 1985, c. 1 (5th Supp.).¹⁴⁸ The national website clearly states that failure to do so is illegal, allowing for real repercussions such as criminal sanctions.

As far as AML/CFT frameworks are concerned, Canada has amended its legislation in 2014 so as to include persons dealing in cryptocurrencies as money services businesses.¹⁴⁹ The full extent of the supporting regulations is still being considered, but it is expected that these money services businesses will have to be registered, do customer due diligence (including beneficial ownership information), keep records and implement internal compliance systems as well as reporting suspicious and certain prescribed transactions.¹⁵⁰ Canada has a similar approach surrounding cryptocurrencies as it is aware that regulation is needed for AML/CFT, but in the same breath acknowledges the need for innovation to be encouraged.¹⁵¹

¹⁴⁵ <https://www.canada.ca/en/financial-consumer-agency/services/payment/digital-currency.html> (accessed: 29 June 2021).

¹⁴⁶ <https://www.canada.ca/en/financial-consumer-agency/services/payment/digital-currency.html> (accessed: 29 June 2021).

¹⁴⁷ <https://www.canada.ca/en/financial-consumer-agency/services/payment/digital-currency.html> (accessed: 29 June 2021).

¹⁴⁸ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 41 – 42.

¹⁴⁹ <https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/canada> (accessed: 28 June 2021).

¹⁵⁰ Financial Action Task Force "Guidance for a Risk-Based Approach: Virtual Currencies" (2014) 15.

¹⁵¹ <https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/canada> (accessed: 28 June 2021).

Accordingly, there is also a reactive approach, whereby regulations are only implemented where they are necessitated.

Both Canada and South Africa use a mixed legal system and the law operates in a similar fashion in both countries.¹⁵² Given the similarities between the Canadian and South African legal systems and that Canada is much more developed, it will be worthwhile to closely monitor its positions and approach to regulating cryptocurrency, which will most likely be appropriate in the South African context.

6.3 China

China's stance towards cryptocurrencies is exceedingly hostile and their approach has been to outright ban most related activities, sparking international news on the radical regulations and operations.¹⁵³ It is one of the few countries globally which opted to issue their own cryptocurrency through their central bank.¹⁵⁴

China's central bank, the People's Bank of China, has classified cryptocurrency as a virtual good and not as currency or legal tender.¹⁵⁵ It has banned financial institutions and payment companies providing crypto-services – even going as far as ordering the police to crack down on any mining activity taking place.¹⁵⁶ Furthermore, the Bank has also banned ICOs, thus sending a clear message to its citizens on China's hostile regulatory approach.¹⁵⁷ Domestic exchange platforms are therefore also illegal and access to foreign exchanges have been blocked together with any websites relating to ICOs.¹⁵⁸ Chinese citizens are not banned from holding cryptocurrency directly, but any method or manner available to do so has been banned.¹⁵⁹ Information surrounding cryptocurrency has also been censored in order

¹⁵² W Tetley "Mixed Jurisdictions: Common Law v. Civil Law (Codified and Uncodified)" (2000) 60 *Louisiana Law Review* 678-738 686-700.

¹⁵³ <https://www.vice.com/en/article/pkb39z/chinas-major-bitcoin-crackdown-is-accelerating-global-shifts-in-cryptocurrency> (accessed: 23 June 2021).

¹⁵⁴ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 43-44.

¹⁵⁵ 43.

¹⁵⁶ <https://www.vice.com/en/article/pkb39z/chinas-major-bitcoin-crackdown-is-accelerating-global-shifts-in-cryptocurrency> (accessed: 23 June 2021).

¹⁵⁷ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 43.

¹⁵⁸ 43-44.

¹⁵⁹ <https://www.reuters.com/technology/chinese-financial-payment-bodies-barred-cryptocurrency-business-2021-05-18/> (accessed: 18 July 2021).

to deter its citizens' interest therein.¹⁶⁰ Although China is one of the most technologically advanced countries in the world, it has made it abundantly clear that it does not consider cryptocurrency to be an asset it is interested in.

Lastly, financial institutions are prohibited from handling transactions where cryptocurrency is present and commercial banks and payment companies must close any cryptocurrency trading accounts.¹⁶¹ This again shows that China will not tolerate dealing in cryptocurrency and these blanket regulations bring almost all cryptocurrency activity within the inimical regulatory scope. This resistance likely stems from a political point of view, as it is argued that any threat to the Chinese economy is a threat to its political system as well.¹⁶²

It is not recommended that South Africa takes such a radical stance towards cryptocurrency as it would completely stifle innovation and likely decrease the tax base. There are however aspects of China's approach that warrant consideration, such as to what extent political views and agendas align with and should influence regulation. Therefore, South Africa may use China's outlook towards cryptocurrency and the consequences thereof to ascertain how and how far the regulatory net should be cast before dealing with undesirable results.

6.4 Japan

Japan has one of the most dynamic climates for cryptocurrency, and the country is at the other end of the spectrum when compared to China. Japan is extremely welcoming towards cryptocurrency and encourages the innovation by recognising it as legal property, with the central bank regulating it.¹⁶³

The Payment Services Act No. 59 of June 24, 2009, acknowledges that cryptocurrency is legal property in Japan, which is not to be confused for legal tender.¹⁶⁴ The IFWG has unfortunately made this error in its 2020 paper, clearly not thoroughly researching Japan's regulations. The IFWG also makes mention of a

¹⁶⁰ <https://intpolicydigest.org/why-china-s-new-mining-censorship-will-affect-more-than-just-crypto/> (accessed: 25 June 2021).

¹⁶¹ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 43-44.

¹⁶² <https://www.voanews.com/east-asia-pacific/voa-news-china/why-china-cracking-down-bitcoin> (accessed: 7 July 2021).

¹⁶³ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 47.

¹⁶⁴ <https://complyadvantage.com/knowledgebase/crypto-regulations/cryptocurrency-regulations-japan/> (accessed: 25 June 2021).

“Virtual Currency Act” passed in 2017, which was in fact an amendment made to the Payment Services Act to include the definitions of crypto assets and not a separate piece of legislation.¹⁶⁵ Unfortunately, neither of these errors were addressed in the IFWG’s 2021 paper.¹⁶⁶

Defining cryptocurrencies as legal property essentially amounts to the same as South Africa’s definition of crypto assets and during 2019 Japan opted to use the term crypto assets as well.¹⁶⁷ By defining cryptocurrencies as legal property, any Japanese crypto exchanges must be registered and comply with AML/CFT duties and obligations – this step is strongly recommended by the IFWG for South Africa as well.¹⁶⁸ The Japanese tax authorities have not yet classified crypto assets, but it is taxing the profits made from it as miscellaneous income.¹⁶⁹

The country has passed numerous legislative revisions during 2020 in order to include crypto asset and bring it in the regulatory ambit.¹⁷⁰ Japan’s friendly support of cryptocurrency has resulted in the innovation contributing to 0.3% of Gross Domestic Product growth as of 2018.¹⁷¹ During 2016 the Bank of Japan established the Fintech Centre, which is “dedicated to supporting healthy development of FinTech”, and this shows a commitment to fully integrate cryptocurrency within the economy.¹⁷² Lastly, Japan is not currently considering launching a central bank cryptocurrency and is only regulating and incorporating decentralised cryptocurrencies.¹⁷³

Japan has taken an incredibly liberal approach, clearly valuing the innovation and the benefits it may hold for its economy, thus attempting to regulate it in a way that protects consumers and the economy whilst still reaping the benefits thereof. Japan’s approach is in stark contrast to that of China’s and again South Africa can

¹⁶⁵ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2020) 47.

¹⁶⁶ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021).

¹⁶⁷ <https://www.sygna.io/blog/japan-crypto-regulation-history-2014-2020/> (accessed: 25 June 2021).

¹⁶⁸ <https://complyadvantage.com/knowledgebase/crypto-regulations/cryptocurrency-regulations-japan/> (accessed: 25 June 2021).

¹⁶⁹ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2020) 47.

¹⁷⁰ <https://www.globallegalinsights.com/practice-areas/blockchain-laws-and-regulations/japan> (accessed: 27 June 2021).

¹⁷¹ <https://www.businessinsider.com/bitcoin-could-be-adding-03-to-japanese-gdp-2017-12?IR=T> (accessed: 27 June 2021).

¹⁷² Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2020) 47.

¹⁷³ 47.

observe the tangible consequences of such a liberal approach and ascertain how it can learn from this approach and apply it to the South African cryptocurrency landscape.

6.5 El Salvador

El Salvador is the first country to pass legislation providing Bitcoin with legal tender status. This monumental decision was celebrated by the country's president, Nayib Bukele (who believes that Bitcoin will reach a hundred thousand dollars before the end of 2021), gifting up to thirty dollars in Bitcoin to any citizen opening a digital wallet.¹⁷⁴ Studies however show that 82.5% of Salvadorans do not want remittances through Bitcoin.¹⁷⁵

This decision comes off the back of the government believing that allowing Bitcoin as legal tender will serve as an economic stimulus and alleviate poverty in the developing country.¹⁷⁶ El Salvador sees almost 70% of its population with no access to financial services and the economy is largely cash driven, with few people having bank accounts.¹⁷⁷ The Bill, which was passed with 62 out of 84 votes and is known as the Bitcoin Law, states that its purpose is to regulate Bitcoin as unrestricted legal tender, which has liberating power, unlimited in any transaction and allowing any public or private natural or legal persons to carry out same.¹⁷⁸ This Bill came into effect on 7 September 2021 and will be the first glimpse of what Bitcoin as legal tender will look like.¹⁷⁹

The Bitcoin Law will purportedly promote and protect private enterprise and generate the conditions necessary to increase national wealth for scores of inhabitants.¹⁸⁰ It accordingly allows for prices to be displayed in Bitcoin and merchants must accept Bitcoin as payment method, tax contributions can be paid in Bitcoin and

¹⁷⁴ <https://www.aljazeera.com/economy/2021/6/25/free-bitcoin-el-salvador-offers-30-of-bitcoin-to-boost-uptake> (accessed: 26 June 2021).

¹⁷⁵ <https://cepr.net/el-salvador-bukele-bitcoin-twitter/> (accessed: 29 June 2021).

¹⁷⁶ <https://www.zdnet.com/article/el-salvador-makes-bitcoin-legal-tender-as-president-looks-to-volcanos-to-mine-crypto/> (accessed: 11 June 2021).

¹⁷⁷ <https://www.reuters.com/world/americas/el-salvador-approves-first-law-bitcoin-legal-tender-2021-06-09/> (accessed: 11 June 2021).

¹⁷⁸ <https://www.reuters.com/world/americas/el-salvador-approves-first-law-bitcoin-legal-tender-2021-06-09/> (accessed: 11 June 2021).

¹⁷⁹ <https://www.reuters.com/technology/bitcoin-become-legal-tender-el-salvador-sept-7-2021-06-25/> (accessed: 26 June 2021).

¹⁸⁰ <https://www.zdnet.com/article/el-salvador-makes-bitcoin-legal-tender-as-president-looks-to-volcanos-to-mine-crypto/> (accessed: 11 June 2021).

exchanges are exempt from paying capital gains tax.¹⁸¹ Furthermore, the country also plans to create 100% renewable cryptocurrency mining facilities, by using volcanos as the energy source.¹⁸² This attention-grabbing step addresses the environmental issue of mining.

South Africa can witness what the effects will be on the Salvadoran economy, as it is also a developing country with similar socio-economic problems. By closely monitoring the implementation of the Salvadoran legislation and the effects on the citizens, South Africa may gain valuable insight as to its own regulations' economic effects by using El Salvador as a case study if it considers affording legal tender status to cryptocurrency in the future.

6.6 Conclusion

The analyses of these countries provide interesting facts on how different authorities deal with cryptocurrency.

These approaches are as thought-provoking as they are insightful, since they provide South Africa with case studies that can sculpt our regulatory response to cryptocurrencies. This will allow South Africa to ensure its response is as optimal and thorough as it can be. Such as the recent development that the Houston Firefighter's Relief and Retirement Fund purchased twenty-five million dollars' worth of Bitcoin and Ether, making it the third Fund of its type in the United States to do so.¹⁸³ This avenue would be worth looking into for South African authorities.

The responses from the countries examined range from hostile to friendly and provide regulation across the spectrum. South Africa has the appropriate risk-based approach, falling somewhere in the middle of the spectrum and attempting to balance mitigating risks and accepting that cryptocurrency may provide future economic stimulation. South Africa is surely not equipped to take El Salvador's approach, nor should it go down the path China has taken. Therefore, South Africa may gain the most fitting insight by looking towards countries such as Canada and Japan for the appropriate regulatory interventions.

¹⁸¹ <https://www.zdnet.com/article/el-salvador-makes-bitcoin-legal-tender-as-president-looks-to-volcanos-to-mine-crypto/> (accessed: 11 June 2021).

¹⁸² <https://www.zdnet.com/article/el-salvador-makes-bitcoin-legal-tender-as-president-looks-to-volcanos-to-mine-crypto/> (accessed: 11 June 2021).

¹⁸³ <https://markets.businessinsider.com/news/currencies/houston-pension-fund-buys-bitcoin-ethereum-crypto-2021-10> (accessed: 22 October 2021).

Chapter 7:

Suggestions and Recommendations

7.1 Introduction

It is trite that cryptocurrencies pose many risks for users, institutions and authorities alike. Therefore, it is crucial that the appropriate regulations and approaches be implemented to mitigate the risks and allow for timely responses. This chapter seeks to recommend and suggest how this can be done and where possible improvements may be made to ensure the response is both effective and efficient.

7.2 Risk-based approach

The IFWG has chosen to adopt a risk-based approach, whereby regulatory actions are undertaken in a way that is commensurate with the risks.¹⁸⁴ This entails balancing potential benefits with the risks and taking into account what the developments of authorities in South Africa and abroad are.¹⁸⁵

This approach largely relies on the monitoring to be comprehensive and accurate. If the IFWG does not adequately monitor and research the current risks associated with cryptocurrencies, the risk-based approach will be compromised, and risks may materialise before they are addressed by regulators. Subsequently, it is suggested that the IFWG meticulously monitor cryptocurrencies and that it keeps abreast of all any developments relating to cryptocurrencies and identify any additional use cases. The risk-based approach is built on the premise that all risks are identified and that the scope of the potential damage is accurately assessed. It has been highlighted how little transparency exists around cryptocurrency and blockchain technology. It is thus recommended that regulators keep this in mind when monitoring cryptocurrency trading volumes, transactions and uses and further attempts be made to increase transparency.

Due to the somewhat lagging response to threats and risks emanating from the risk-based approach it is recommended that authorities ensure they have a long-term

¹⁸⁴ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 29.

¹⁸⁵ 29.

risk forecast that is monitored closely and regularly, including making the necessary updates. This will allow for a timely response to the more serious systemic risks as well. Where threats to the economy become a concern, the risk-based approach may fail to allow for a robust response to mitigate these critical systemic risks. The regulators should therefore consider addressing these concerns well in advance and create a regulatory package that can be implemented before these risks materialise, to ensure the integrity of the monetary policy and national payment system.

It is recommended that the IFWG stay the course with the risk-based approach for the time being, but it may become necessary in the future to take a more proactive approach and to adjust the strategies accordingly. Furthermore, the neutral stance South Africa has toward cryptocurrencies is appropriate at present, but it is recommended that the IFWG keeps on monitoring the situation as laid out in its report to ascertain if its stance should be adjusted to a more welcoming or hostile approach, based on the risks and benefits.

7.3 Current regulations and landscape

The current and proposed regulations are hugely advantageous in mitigating risks related to the use cases of cryptocurrencies. Some of these regulations have been implemented, but most of them are still in the process thereof.

The lack of implemented regulations is undoubtedly a potential issue, as risks can only be mitigated where regulations are in full force and effect. It is therefore highly suggested that the proposed regulations be implemented in a timeous manner. It is clear that cryptocurrencies are here to stay and without operational regulations, or with limited regulations, cryptocurrency related legal disputes may vastly increase with no recourse for aggrieved parties.¹⁸⁶ Furthermore, criminals may take advantage of the fractional regulatory field that currently exists. The proposed regulations should therefore come into full force and effect before the lack thereof is exploited. This suggestion includes that the Cybercrime Act should come into force as soon as possible.

¹⁸⁶ National Treasury “User Alert Monitoring of Virtual Currencies” (2014) 1-4.

The second issue with the current landscape is the lack of expertise when it comes to the boots on the ground and courts.¹⁸⁷ South African law enforcement lacks the necessary know-how when it comes to cybercrimes. Accordingly, it is recommended that training should be given to law enforcement on cybercrimes and how to prevent, investigate, prosecute, adjudicate and sentence the accused.¹⁸⁸ Even if regulations are implemented, they will be rendered toothless if the law enforcement does not respond in the suitable manner to cryptocurrency related crimes. The training should thus be comprehensive enough to equip law enforcement to respond aptly to the different types of cybercrimes. The type of response is especially important since cybercrimes are time sensitive and extremely easy to cover up.¹⁸⁹

Thirdly, it is recommended that increased efforts should be made to inform South Africans of the risks associated with cryptocurrencies. The IFWG emphasises that it is necessary for users to know and understand the risks and for citizens to be informed to protect them from scams and fraud.¹⁹⁰ It is highly recommended that this should be the case, but there have been very few attempts to disseminate information in this regard. User warnings are placed on government sites, but these sites are seldom visited by the average South African. A different approach is therefore suggested, whereby information and notices should be made publicly available in a way that will reach greater numbers of the population.

Lastly, it may prove valuable to include different stakeholders in regular consultations, such as commercial banks. As the leading authority of cryptocurrencies in South Africa, the IFWG may gain valuable insight and new considerations when engaging experts on cryptocurrencies, ICOs and commercial banks for example. This provides an additional method of monitoring cryptocurrencies, without using government resources.

These recommendations and suggestions will allow for an increasingly thorough approach to regulation and addresses the practical aspect of investigation and prosecution, which will allow for a holistic and inclusive approach.

¹⁸⁷ S Dlamini & C Mbambo “Understanding policing of cyber-crime in South Africa: The phenomena, challenges and effective responses” (2019) *Cogent Social Sciences* 6-7.

¹⁸⁸ 10.

¹⁸⁹ 6.

¹⁹⁰ Intergovernmental Fintech Working Group Crypto Assets Working Group “Position on Crypto Assets” (2021) 35.

7.4 International considerations

The IFWG in its 2020 paper included a comprehensive list of countries and their cryptocurrency stances and regulations.¹⁹¹ This list was not included in the 2021 version of the report, even though great strides were made by some countries over the last year, such as Bitcoin becoming legal tender in El Salvador.¹⁹² Furthermore, the 2020 report states that Japan has made cryptocurrency legal tender, which is not the case.¹⁹³ Mistakes such as these misinform users and may convey that cryptocurrencies are more widely accepted as what they really are. It is therefore suggested that the IFWG ensures its research is thorough and the reports are accurate and reliable. If the IFWG makes mistakes, it may be to the detriment of the very consumers it is attempting to protect.

The cross-border nature of cryptocurrencies has been referred to numerous times throughout this dissertation and it poses various risks and difficulties for regulators. It is recommended that South Africa should implement open communication channels with other countries to align responses or to create multinational working groups to ensure AML/CFT measures are effective. To that end, it is also suggested that a multinational or international task force be considered to address crypto-crimes. This will assist in improving expertise and sharing of information to ensure criminals are identified and brought to justice.

Lastly, it is essential that South Africa closely and precisely monitor other countries' approaches and regulations, as well as the effect they have on the risks and potential benefits of cryptocurrencies. This will ensure that South Africa has an informed approach when it regulates cryptocurrencies. The broad recommendation is to ensure that South Africa adequately communicates, monitors and collaborates with other countries to ensure our response is balanced and thorough.

These recommendations and suggestions will aid in moulding South Africa's response and to guarantee that the best possible response is crafted and implemented, by collaborating with and learning from other countries.

¹⁹¹ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 41-52.

¹⁹² <https://www.aljazeera.com/economy/2021/6/25/free-bitcoin-el-salvador-offers-30-of-bitcoin-to-boost-uptake> (accessed: 20 August 2021).

¹⁹³ Intergovernmental Fintech Working Group Crypto Assets Working Group "Position on Crypto Assets" (2020) 47.

7.5 Conclusion

When viewed holistically, it is clear that South Africa has made a serious attempt to regulate cryptocurrencies in the appropriate manner. The approach taken by South Africa's IFWG has been comprehensive and deals with most issues known to regulators at this stage. Due to the novelty of cryptocurrencies however, it is expected that there may be *lacunae* in the approach and that improvements can be made.

The suggestions and recommendations made herein seek to address the spaces regulators have not yet addressed or where they can bolster their current position. These suggestions and recommendations are not a closed list and are anticipated to substantially grow with the increased use of cryptocurrencies. The most important recommendations are to stay abreast of any developments, to consume relevant information, monitor the situation as close as possible and dynamically address risks.

Chapter 8:

Conclusion

8.1 Findings of the current landscape

Throughout each chapter, a part of the current setting in which cryptocurrencies operate has been elucidated. By analysing the setting, many details have emerged and a few specific points have become clear.

The first is that cryptocurrencies are complex, and the nature thereof makes it inherently difficult to regulate. By clarifying how cryptocurrencies operate, it has become clear that the technology is not like any technology authorities have worked with before. It has the ability to circumvent the central authority, but still keeps the integrity of the entire operation through the distributed ledger technology. Furthermore, a lack of understanding has made it even more difficult to understand where the risks and benefits are. It is therefore paramount that adequate knowledge is consumed before any regulations are implemented and that the relevant authorities collaborate in an effort to satisfactorily bring cryptocurrencies into the regulatory net.

The second is that South Africa has taken an active approach in mitigating risks and attempting to balance risks and benefits. This has been done by the IFWG, which comprises of all the relevant institutions and authorities. The IFWG has made suitable regulatory recommendations and has shown a cohesiveness between its members in addressing the way in which cryptocurrencies should be regulated. South Africa's neutral and risk-based approach has exhibited a willingness to encourage innovation and to look at new ways to strengthen our ailing economy, whilst still being committed to addressing risks.

Thirdly, large parts of the regulatory basket have not yet been addressed by South Africa. The IFWG attempts to gain a holistic view of cryptocurrencies, but the picture has unpainted canvas as it presently stands. The IFWG makes no mention of the practical aspect of the regulations, such as training, nor does it address how to solve the cross-border issues. Furthermore, there is a dissonance between proposing regulations and the real implementation thereof, leaving an increasing number of persons without the necessary legal protection. Lastly, there are ways in which cryptocurrencies, blockchain technology and distributed ledger technology can

operate that we have not yet seen or explored and will only become prevalent in the years to come.

8.2 The way forward

Clearly, this is only the beginning stages of integrating cryptocurrencies in our economy. There are bound to be growing pains, but the success of the integration will largely rely on how we approach and adapt in the future, if done successfully individuals and countries may realise great profits.

South Africa has undoubtedly taken an interest in cryptocurrencies and has made strides in regulating it. The crucial part now is to implement these regulations and to keep on monitoring as many aspects of cryptocurrency as possible. The way forward is still highly speculative, and some risks may never materialise, whereas others may be present without regulators even being aware. To that end, it remains of paramount concern that our regulators keep apprised of any occurrences and that where action is needed it is not only taken in a timely manner, but also in an effective manner.

It is evident that cryptocurrencies will eventually form part of our everyday lives and that many legal disputes will arise in years to come. The best way forward will be to protect users and to tap the benefits cryptocurrencies hold for our economy.

8.3 Conclusion

The only way society can move forward is by inventing something new. It can hardly come as a surprise that something like cryptocurrencies have come into existence. It is undeniable that, if approached correctly, cryptocurrencies can have major impacts on economies and income levels in future years. The way in which we integrate this innovation into our lives will dictate how much of the benefits we will be able to reap. Authorities accordingly have a great responsibility to treat cryptocurrencies in the best way possible.

The landscape for cryptocurrencies is still highly speculative and a lot of the risks are merely on the horizon. As time goes by and these risks come closer, we will be able to better view them and address them accordingly. The best way forward, for now, is to maintain one eye on the horizon and keep a balanced and cautious approach.

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