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Prevention of Money-Laundering in Slovenia related to Cryptocurrency services: "Already ahead of the MLD5"

Crypto assets and among them cryptocurrencies, which this article focuses on, have proven themselves as an eminent opportunity in many aspects of the new digital economy, giving birth to new innovative enterprises and enabling exchange of value in a decentralized manner. This is also evident in Slovenia, being a well-known hub of successful professionals in the crypto world. This glorious future aside, attention must be paid to the fact that cryptocurrencies can also present an anonymous medium for money-laundering and financing of terrorism, which shall be tackled on the EU level by the adoption of the draft fifth money laundering directive ("*MLD5*")[1].

The latter introduces the definition of "virtual currency" and imposes the exercise of anti-money laundering and counter terrorism financing (AML) measures upon certain services related to virtual currencies such as exchange platforms and providers of custodial wallets for cryptocurrencies. The member states must transpose the MLD5 by 10 January 2020. Until today, the transposition level has been rather scarce and Slovenia has also not, as of yet, transposed the MLD5. However, the applicable Slovenian Prevention of Money Laundering and Terrorist Financing Act ("*ZPPDFT-1*") already contains the definition of virtual currency

[1] Directive Of The European Parliament And Of The Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing

closely resembling the one from MLD5, and further imposes certain AML measures regarding services involving virtual currencies, similar to those envisaged in MLD5. Therefore, it is important to establish who the law affects already in the currently applicable text.

ZPPDFT-1 requires from entities engaging in "*(i) issuance and (ii) management of virtual currencies, including (iii) exchange services between virtual currencies and fiat currencies*" to implement anti money-laundering and counter terrorism finance policies, together with detailed controls and processes for reporting suspicious transactions. Virtual currencies are defined as "*digital representation of value that is issued by a natural or legal person other than a central bank or a public authority, that is used as a means of exchange and can be transferred, stored and traded electronically, and is not necessarily attached to traditional (fiat) currencies and can represent a direct means of payment between the entities accepting it*".

The law's reference to issuance of virtual currencies (item (i) above) and to exchange of fiat currencies for virtual currencies and vice versa (item (iii) above) is rather clear-cut, leaving no doubt that such a provider must adhere to anti money-laundering and counter terrorism financing policies. On the other hand, it is less straightforward what is to be understood under "management" of virtual currencies (item (ii) above). Common services related to existing virtual currencies include, inter alia, exchange services between different virtual currencies and storage of cryptocurrencies in hosted wallets or other custodian services. There is currently no publicly available information on practice of the regulators, neither have any formal opinions or guidelines been published yet.

Regarding the *exchange services between different virtual currencies*, it is likely that they do not fall within the scope of services subject to AML measures, understood under the term "management". There are two points to this argument. *First,* the provision of ZPPFT-1 regarding exchange services is clearly limited to exchange between virtual *and fiat* currencies, despite the fact that it could easily contain a broader wording. *Second*, the critical moments in the process of money-laundering are the "disappearance of dirty money" and "reappearance of clean money", which, by employment of virtual currencies, happens when a fiat currency is transformed into a virtual currency and ultimately the other way around. Additionally, we have been informally informed by the Slovenian regulators that virtual currencies should not be considered "money" or "e-money", which is in line with what the MLD5 also expressly confirms in its introductory recitals.

Regarding the *digital wallet and/or custody services*, our experience with the Slovenian regulators implies that the term "management" should be understood broadly, also including

any wallets able to store virtual currencies or custody services. Considering that the legislator employed a rather broad term “management” in the law, it can be reasonably agreed that this breadth of reach of ZPPDFT-1 was the legislator’s intention, i.e. to also include hosted wallet and custody services.

Considering the above, while the notion of “management” of virtual currencies remains open for interpretation regarding potential new innovative services, we can conclude that when conducting business in Slovenia, enterprises engaging in exchange services between virtual and fiat currencies (but not between different virtual currencies), as well as providers of hosted wallets and custody services, should take care of the AML and counter terrorism financing rules, already ahead of the MLD5.

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