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The Regulatory Impact of the Ukrainian War

The Digital Regulator



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Executive summary

The decision to economically sanction Russia, following its military invasion of Ukraine on 24 February 2022, has led policy makers and regulators to worry that cryptoassets may be used to evade such international sanctions. The G7 and some other countries, such as Switzerland and Singapore, have made it clear that compliance with the sanctions also apply to transactions in cryptoassets and the operations of related service providers. On 21 April, the International Monetary Fund and the US Treasury concluded that there was no evidence that cryptoassets were being used to evade sanctions in any material way – this outcome being driven by the structure and nature of crypto markets and the compliance efforts made by exchanges. However, even though the concerns turned out overrated, there is now a sense of urgency to regulate the crypto industry internationally, causing several crypto-leading countries to take initiatives to protect their status and contribute to the cause. Centralised cryptoexchanges have stepped up their compliance efforts, and authorities in the US have renewed efforts to regulate them. As a legacy of the ongoing war, regulators will continue to expedite the extension of their perimeter to the governance of decentralised cryptofinance platforms and further discourage the use of anonymous cryptocurrencies. On a global scale, policy makers will focus on establishing rapidly comprehensive standards for cryptoassets in the face of a growing ‘cryptoization’ of emerging markets. On balance, the regulatory discussion, analyses, and actions that the ongoing war has triggered will not undermine the broad adoption and development of cryptofinance, but foster its sustainable integration instead.

During the last few weeks, the Central African Republic followed El Salvador to become the second country to make bitcoin legal tender. The Swiss National Bank ruled out the possibility to hold bitcoins on its balance sheet. Several jurisdictions, such as Singapore, Australia, and Gibraltar, reported important milestones in the development of regulatory frameworks for cryptofinance, and a handful of African countries in moving towards a central bank digital currency (CBDC).

Early concerns that the use of cryptoassets might undermine the effectiveness of sanctions have turned out to be overrated, due to the structure of crypto markets and compliance efforts by exchanges.

The Ukrainian war is accelerating the development and implementation of global cryptofinance standards.

1. The war and its regulatory legacy

Following the military invasion of Ukraine by Russia on 24 February 2022, the international community decided to economically sanction Russia, targeting individuals, banks, businesses, monetary exchanges, bank transfers, exports, and imports, excluding major Russian banks from SWIFT (Society for Worldwide Interbank Financial Telecommunications), and freezing the assets of the Russian Central Bank. We briefly review the initial concerns among policy makers and financial regulators that cryptoassets could be used to evade the sanctions, and examine the actions taken by international bodies and national authorities, as well as by centralised cryptoexchanges, to prevent this from happening. In addition, we appraise the analyses of the nature and structure of crypto markets that suggested cryptoassets could be used to evade sanctions in any material way. Over time, regulators have turned their attention to decentralised finance (DeFi) platforms, the potential use proof-of-work mining to generate revenues and weaken sanctions, and the challenges raised by the increased ‘cryptoization’ of emerging economies.

- **Early concerns and policy reactions**

On 25 February, the European Central Bank ([ECB](#)) expressed concerns about the use of cryptoassets to evade the freshly imposed international sanctions, and emphasised that compliance with sanctions applied to transactions in cryptoassets and the operations of related service providers. It called for an acceleration of the development and implementation of the crypto-regulatory framework, or Markets in Crypto-assets regulation. On 1 March, the [US](#) government (White House and Treasury) asked US-based businesses and individuals not to support crypto transactions addressed to specific Russian individuals and banks. On 4 March, the [G7](#) and the [EU](#) announced measures to restrict the use of cryptocurrencies to evade sanctions. On 12 March, the [US](#) Treasury made clear that it would take legal action against the use of virtual currencies to circumvent economic sanctions. The first impact of the ongoing war on cryptofinance regulation has, therefore, been a sense of urgency to accelerate the momentum to regulate cryptofinance, and a clear call for compliance action.

- **Cryptonations initiatives**

On 5 March, the [Swiss](#) federal government announced freezing cryptoassets owned by Russian citizens and businesses. This measure came on top of the penalties decided at the EU level, which Switzerland adopted. On the same date, [Singapore](#) and [Japan](#) announced sanctions against the Russian Federation that would include prohibiting digital payment token service providers from supporting transactions aimed at circumventing sanctions. The [UK](#) followed suit on 11 March by mandating explicitly crypto firms to comply with the sanctions. A second effect of the ongoing war on cryptofinance regulation has taken the form of a series of measures that the main cryptofinance hubs have adopted against cryptoactors, to protect their own status and contribute to the effectiveness of the sanctions.

- **Cryptoexchanges in focus**

In early March 2022, [Coinbase](#) and [Binance](#) responded to the regulatory expectations by clarifying their [commitment](#) to complying with the sanctions. They reported they had enhanced monitoring and detection of attempts to evade the sanctions through cryptoasset transactions, eventually preventing such users from using the exchange services. [Binance](#) also stopped accepting Mastercard and Visa cards held by Russians as a way to interact with the exchange. While evidence showed that Russians had been buying more crypto following the sanctions, it is clear that it was more as a response to the desire to fight the depreciation of the ruble rather than to evade sanctions. During the first half of April 2022, the US Securities and Exchange Commission ([SEC](#)) pushed for more oversight of centralized cryptoexchanges and announced a cooperation with the Commodity Futures Trading Commission (CFTC) in the supervision of such platforms. The [SEC](#) confirmed its intention to regulate cryptoexchanges, like traditional securities exchanges. A third consequence of the ongoing war on cryptofinance regulation has therefore been a push to centralised cryptoexchanges to accelerate know-your-customer (KYC) and anti-money-laundering (AML) compliance, and monitoring of related transactions.

- **Overstated worries**

Analysts doubted if cryptocurrencies could be used effectively to evade sanctions in a material way. They argued that cryptocurrencies are insufficient as an asset class to absorb the sheer damage caused by the sanctions, and that their large-scale use (by states, institutions, and individuals) would exacerbate price volatility. Moreover, individuals using cryptos to evade sanctions would have to deal with the traceability of their transactions. It, thus, became clear that the Russian state, institutions and individuals were unlikely to have been using cryptocurrencies to evade international sanctions. On 21 April, the International Monetary Fund (IMF) concluded that there was no strong evidence on the use of cryptocurrencies by governments, companies, or individuals to massively evade international sanctions. The statement aligned with the US Treasury view that cryptocurrencies cannot be used on a large scale to evade the sanctions. The compliance efforts deployed by the main cryptoexchanges are sure to have contributed to this outcome.

- **Regulatory legacy**

Next to fuelling a sense of urgency on the need to regulate cryptofinance, leading key crypto nations to implement immediate measures, and triggering major cryptoexchanges to step up compliance, the regulatory legacy of the ongoing war extends to the mining of PoW coins (energy intensive) and associated concerns that it may be used by Russia to divert its vast energy resources, generate revenues and evade sanctions. This legacy includes fears that the ongoing war may lead to a more widespread use of cryptoassets in emerging markets and through DeFis. These concerns led the IMF, in its annual report, to call for regulatory action in the form of comprehensive global standards for cryptoassets, including governance schemes for DeFi platforms, and the use of anonymous cryptocurrencies. On that score, on 31 March, the EU Parliament approved measures to outlaw anonymous crypto transactions.

The need to ensure the effectiveness of international sanctions against Russia has increased the sense of urgency to regulate the industry, led several crypto-leading countries to take concrete measures to protect their status and contribute to the cause, triggered centralised cryptoexchanges to step up KYC /AML compliance and transactions monitoring efforts, and authorities in the US to renew efforts to regulate cryptoexchanges similarly to traditional securities exchanges. The war has shown that cryptocurrencies can be a valid tool to facilitate transactions in warzones; by 12 March, donations to Ukraine in cryptocurrencies surpassed USD 100 million, while Ukraine had spent cryptos to meet about 20% of its USD 30 million-worth military equipment expenses. The regulatory legacy of the ongoing war is taking the form of increased focus on DeFi governance and of an acceleration of the (further) development, and implementation of crypto-regulatory frameworks around the globe, more broadly. We anticipate the net effect of this consequences to be supportive of, rather than undermining, the broad adoption and development of sustainable cryptofinance.

2. Other noteworthy developments

The momentum to develop crypto-regulatory frameworks continued in several jurisdictions, including Singapore, Australia and Gibraltar.

- Singapore augmented the regulatory powers of its monetary authority (MAS) and is poised to strengthen the licensing process. Virtual asset service providers are now obliged to apply for licenses, and the Financial Services and Markets Bill assigns new powers to MAS, including the ability to prohibit persons considered unfit to perform key roles from working in payments and risk management. The MAS also anticipated strengthening the licensing process for digital asset service providers to ensure the country remains innovative but sustainable.
- Georgia's central bank announced it is working on a regulatory framework for crypto, and the Capital Markets Authority of Oman said it would include real estate tokenisation into its virtual asset regulatory framework. Australian authorities have outlined a regulations roadmap for cryptocurrencies and digital asset companies, while Brazil's Senate passed a bill governing cryptocurrencies to set the stage for the creation of a regulatory framework for the country's crypto industry. Gibraltar introduced new laws for blockchain companies aimed to curb illegal financial activities, the Telecommunications Authority of Nepal warned that crypto activities are illegal and all related websites and apps are prohibited, and Panama passed a law supporting the digital economy, blockchain, and cryptoassets for improved financial inclusion.

Several countries reported progress in the adoption of CBDCs, even as the Bank for International Settlements (BIS) stressed the positive effect of CBDCs on financial inclusion.

- Namibia's central bank has announced plans to develop a CBDC, positioning it as an electronic version of central bank money, and anticipates wide adoption. Cameroon is considering issuing a CBDC based on blockchain solutions powered by The Open Network. Brazil's central bank confirmed it would run a pilot test of CBDC with a view to completing the testing by the end of the year. Russia's central bank also plans to test a digital ruble this year, though the move is not directly linked to the actual issuance of such CBDC.
- In a study, the BIS concluded that existing barriers to financial inclusion could be addressed with the introduction of a CBDC. The BIS considers the following as current challenges to financial inclusion: geographical barriers, institutional / regulatory factors (such as a lack of public goods such as identity credentials and consumer protection, as well as informality), economic and market structure issues, such as limited competition, vulnerability, such as barriers of age and gender, lack of education and financial literacy, and low trust in existing financial services.

A second country followed El Salvador in making bitcoin legal tender, while the Swiss central bank ruled out the possibility to hold bitcoins on its balance sheet. In the US, a third bitcoin futures exchange traded fund (ETF) was authorised, while the approval of the first bitcoin spot ETF is not in sight.

- The Central African Republic made bitcoin legal tender, becoming the second country after El Salvador. The Swiss National Bank (SNB) denied plans of buying and holding bitcoin on the bank's balance sheet. The SEC authorised Arca and Teucrium's bitcoin futures ETF.

3. Conclusion

History often progresses in stages, and the regulation of cryptofinance is no exception. The Ukrainian war has accelerated the process of regulating cryptoexchanges, the development and implementation of domestic regulatory frameworks and global standards, and led many countries to take immediate measures. The integration and broad adoption of cryptofinance requires the industry to be regulated in a sustainable way. The nature of the regulatory policy decisions discussed above indicates that the legacy of the war will not undermine, but rather support the development of cryptofinance.

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