Blockchain & Cryptocurrency Regulation

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Country chapters

Malta

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Government attitude and definition

Malta has positioned itself as a key player in the world of Distributed Ledger Technologies ("**DLTs**"). The Government of Malta, local regulators and other stakeholders have adopted an open and collaborative approach towards this sphere, rooted in striking the right balance between maintaining Malta's perception as a jurisdiction of repute, integrity and financial stability, and the desire to foster a business and legal environment conducive towards innovative technologies, products and services.

The first half of 2018 has been characterised by Malta's clear determination to promulgate regulation that is a first of its kind. A collective effort, spearheaded by the Parliamentary Secretariat for Financial Services, Digital Economy and Innovation together with the Malta Financial Services Authority (the "**MFSA**"), has enabled Malta to carry out the necessary reforms to formulate an innovative yet robust regulatory and legal framework designed to meet the commercial, technical and technological peculiarities inherently characterising blockchain and cryptocurrencies. The Government of Malta has led by example and has expressly stated that it is resolute in establishing Malta as the "Blockchain Island". To this end, it has set up a number of blockchain-related innovative projects with the intention of attracting big industry players to the island (see "Promotion and testing", below).

Following a series of public consultations with the industry throughout the course of the past year, the willingness of the Government of Malta to digitalise Malta's economy and cement its position as a jurisdiction of choice for innovators has culminated in the formal enactment of a comprehensive set of three complementary legislative acts at the beginning of July 2018. These acts are:

(i) the Malta Digital Innovation Authority Act (the "**MDIA**");

(ii) the Innovative Technology Arrangements and Services Act (the "**ITAS**"); and

(iii) the Virtual Financial Assets Act (the "**VFAA**"),

(collectively hereinafter referred to as the "**Digital Innovation Framework**").

In essence, this means that market participants in the blockchain and cryptocurrencies industries may establish or operate in or from Malta, and benefit from a higher degree of legal certainty – which will have a knock-on beneficial impact through enhanced trust, marketability, legal certainty and consumer adoption.

Cryptocurrency is not treated as money or given equal recognition with domestic or foreign fiat currency in Malta – or at least, not as yet. As at the date of writing, there are no cryptocurrencies that are backed by the Government of Malta or the Central Bank of Malta.

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Cryptocurrency regulation

Following the enactment of the VFAA, cryptocurrencies may be regulated under the VFAA or existing financial services legislation, including but not limited to the Markets in Financial Instruments Directive II ("**MiFID II**"), the Investment Services Act (Chapter 370 of the Laws of Malta) and the Financial Institutions Act (Chapter 376 of the Laws of Malta). Which regulatory regime (if any) will apply is dependent on the classification of the asset in question.

Malta's Digital Innovation Framework sets out four possible categories of Distributed Ledger Technology Assets ("**DLT Assets**"), which may include cryptocurrencies. These are:

(i) Electronic Money;

(ii) Financial Instruments (albeit that are intrinsically dependent on, or utilise, Distributed Ledger Technology);

(iii) Virtual Tokens (more commonly referred to as Utility Tokens); or

(iv) Virtual Financial Assets ("**VFAs**").

The classification of the DLT Asset in question into one of the four categories listed above will be mutually exclusive therewith.

The VFAA introduces a mandatory regulatory regime that regulates DLT assets and related service providers, including, amongst others, Initial Virtual Financial Asset Offerings ("**IVFAOs**") issuers (more commonly known as ICOs), and Virtual Financial Asset Exchanges ("**VFA Exchanges**") (more commonly referred to as Crypto-Exchanges). The VFAA also introduces a new class of intermediaries, to be known as Virtual Financial Asset Agents ("**VFA Agents**").

The crux of the matter is determining whether the asset in question falls within the scope of the VFAA and is therefore prone to being regulated thereunder. In this respect, the VFAA empowers the MFSA to introduce a test, to be known as the Financial Instrument Test (the "**Test**"), for the purpose of classifying a DLT Asset as one of the aforementioned classes of DLT Assets and thereby determining whether the DLT Asset would be regulated under the VFAA, existing financial services laws or neither of the two (remaining unregulated). The Test was published in July 2018 along with a guidance note on how to interpret and apply its steps. The Test must be carried out on a case-by-case basis. The VFAA indicates that it will be the task of the VFA Agent (along with the VFA issuer if the Test is being carried out in relation to an IVFAO) to carry out this assessment with respect to a DLT Asset when:

(i) an issuer intends to launch an IVFAO to the public in or from within Malta;

(ii) an issuer admits the VFA to trading; and/or

(iii) a service provider intends to conduct VFA-related services.

The Test will firstly determine whether the DLT Asset is to be classified as a Virtual Token and therefore fall outside the scope of regulation. A Virtual Token is defined as being a form of digital medium recordation whose utility, value or application is restricted solely to the acquisition of goods or services, either solely within the DLT platform on, or in relation to which, it was issued or within a limited network of DLT platforms (but not DLT exchanges).

If the DLT Asset is determined not to be a Virtual Token, one must move on to the second stage of the Test wherein it will be determined whether the DLT Asset falls within the scope of existing financial services legislation. If the VFA Agent determines that the DLT Asset does indeed fall within the scope of existing financial services legislation, then the issuer or service provider in question would be required to comply with the regulatory regime

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applicable to financial instruments or electronic money, depending on the characteristics of the asset. On the other hand, if it is determined that the DLT Asset does not fall within the scope of existing financial services laws (or would be considered a Utility Token as aforesaid), the token automatically falls into the last stage of the Test, whereby the token would be deemed to be a VFA, and therefore, due to be regulated by the VFAA.

If a DLT Asset is determined to be a VFA, VFA-related service providers will be required to adhere to the provisions of the VFAA. For example, an issuer of an IVFAO offered to the public in or from Malta must register its white paper with the MFSA, and the white paper must comply with the conditions set out in the First Schedule of the VFAA. Furthermore, a VFA service provider as listed in the Second Schedule of the VFAA (such as VFA exchanges) offering a VFA service in or from Malta will be required to obtain a licence from the MFSA before it may commence its operations.

Sales regulation

The sale of cryptocurrencies such as Bitcoin or other tokens may be regulated by securities laws. In order to determine whether the sale of tokens would be regulated by securities laws, according to the VFAA each DLT Asset must be assessed to determine whether the said DLT Asset falls within the scope of (i) existing securities laws or (ii) the VFAA, or be unregulated. Should the DLT Asset fall within the scope of existing securities laws by virtue of it being classified as a Financial Instrument following completion of the Test, then that token must comply with securities laws.

There are no commodities laws regulating the sale of cryptocurrencies or other tokens as at the date of writing.

Taxation

At present, there are no rules or guidance in place that specifically treat the taxation of cryptocurrency in Malta, whether from an income tax, duty or VAT perspective. In the absence of specific rules, the general rules and principles of Maltese tax legislation apply.

By way of background, the Income Tax Act (Cap. 123 of the laws of Malta) distinguishes between receipts that are of an income nature and receipts that are of a capital nature. Receipts that are of an income nature are in principle subject to Maltese income tax either: (i) at the rate of 35% if the recipient is a body of persons; or (ii) at progressive rates – up to the maximum level of 35% – if the recipient is a natural person. Gains that are of a capital nature are subject to Maltese income tax either: (i) at the fixed rate of 35%; or (ii) are not taxable at all. The Income Tax Act does not define "income", rather, it attempts to provide a meaning of the term by non-exhaustively listing several sources of revenue that are considered to be income, such as gains or profits from any trade, business, profession or vocation. On the contrary, the Income Tax Act exhaustively lists those capital gains that are within scope of income tax. Cryptocurrency is currently not listed as an asset that is subject to income tax on any capital gains.

Whether a receipt is considered to be of an income nature (that is, generally arising from a trade, business, profession or vocation) or of a capital nature depends on the so-called "badges of trade". These are indicators developed by UK jurisprudence and accepted by both the Maltese tax authorities and courts. The indicators point towards a profit or gain being derived from a trading activity and therefore having the nature of income, as opposed to capital. Important indicators of profits derived in the course of a trade (and therefore taxable as income) include, amongst others: the frequency of transactions; the existence of

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a profit-seeking motive; the nature of the asset; whether supplementary work and marketing has been conducted; and the length of the ownership.

In applying the above principles to transactions in cryptocurrency, profits derived from a transaction would be characterised as income of a trading nature or income of a capital nature dependent on subjective factors such as: (i) the intention of the acquiror when the cryptocurrency was bought; (ii) the period of time that the cryptocurrency was held; (iii) the price at which the acquiror entered the market and the price-trend at the moment of entry; and (iv) the price of disposal and the price-trend at the moment of exit.

For instance, if an individual acquired bitcoins in 2012 when the acquisition value was substantially lower than its price at the end of 2017 and has held the bitcoins through the currency's highs and lows but decides to dispose of the holding in 2018, it is likely that the cryptocurrency was held, and will be perceived to have been held, as a long-term investment. The receipt derived from the transfer of such cryptocurrency would likely be treated as income of a capital nature. As discussed above, capital gains from the disposal of cryptocurrency do not currently fall within scope of taxable capital gains and therefore no tax should be payable by the transferor. On the other hand, if an individual consistently trades in Bitcoin, on an ongoing basis, such activity is susceptible to having any receipts derived from the transfer of the cryptocurrency treated as income from a trading activity and taxable at the relevant rate. It is pertinent to note that there is currently no official position in Malta that sheds light on the period of time that should lapse for the holding of the cryptocurrency to be treated as being held for capital purposes as opposed to trading purposes. In view of the above, the nature of the income derived from cryptocurrency would therefore need to be assessed on a case-by-case basis.

Insofar as duty payable by the acquiror of the cryptocurrency is concerned, there are currently no provisions in the Duty on Documents and Transfers Act (Cap. 364 of the laws of Malta) which impose a duty charge on the transfer of cryptocurrency.

From a VAT perspective, we expect the Maltese tax authorities to follow the Court of Justice of the European Union's pronouncements in the *Hedqvist* case (C-264/14) should and if a similar domestic situation arise. Thus, the exchange of bitcoin for traditional currency and vice versa, which is effected for consideration, would likely be seen as a supply of a service but would ultimately be exempt from VAT.

In order to complement the recent domestic developments in blockchain regulation as discussed in the section "Cryptocurrency regulation" above, industry and practitioners expect the Maltese tax authorities to issue guidance on the income tax, duty and VAT treatment of transactions in cryptocurrency in the near future.

Money transmission laws and anti-money laundering requirements

Malta's main legislation regulating anti-money laundering and the countering of the funding of terrorism ("**AML/CFT**") are: (i) the Prevention of Money Laundering Act (Chapter 373 of the Laws of Malta) ("**PMLA**"); and (ii) the Prevention of Money Laundering and Funding of Terrorism Regulations (Subsidiary Legislation 373.01) ("**PMLFTR**"). These legislative instruments transpose the requirements of the Fourth Anti-Money Laundering Directive (Directive (EU) 2015/849).

Persons carrying out either a "relevant financial business" or "relevant activity" will be considered to be a subject persons under the PMLA and PMLFTR and, therefore, they must adhere to the obligations therein relating to subject persons. In addition, subject persons shall also comply with the Implementing Procedures, and other guidance, as issued and

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updated from time to time by the AML/CFT regulator in Malta, the Financial Intelligence and Analysis Unit ("**FIAU**").

With specific reference to issuers of cryptocurrencies and related service providers, the VFAA provides that: (i) an issuer; (ii) a VFA licence holder; and (iii) a VFA agent under the VFAA, shall be considered as a subject person. Finally, in the white paper required to be registered with the MFSA for the purposes of an IVFAO to the public, or the admission thereof on a DLT Exchange, the issuer is required to include a description of the issuer's adopted white-listing and anti-money laundering and counter financing of terrorism procedures in terms of the PMLA and any regulations made and rules issued thereunder. VFA issuers, licence-holders and agents are also required to abide by any sector-specific guidance that may be issued by the FIAU from time to time.

Promotion and testing

In March 2018, the Malta Gaming Authority ("**MGA**") released guidance on the use of DLTs and the acceptance of Virtual Currencies ("**VCs**") in the gaming sector through the implementation of a sandbox environment. The sandbox commenced early in Q2 2018 and will last for a period of six months. The principal objective of the MGA's sandbox is to consider allowing the use and implementation of DLTs and VCs by gaming and gambling operators licensed by the MGA.

In order to safeguard players and the gaming ecosystem, either of two distinct implementation scenarios is deemed acceptable:

(i) a "single wallet system"– in the first scenario, the operator has a maximum of one wallet for every supported cryptocurrency. The players issue deposits to the address of that wallet and use their account with the operator to notify that they just made a deposit from a certain wallet's address. If the deposited amount respects the "maximum amount" and any deposit limit previously set by the player, the funds are kept in the operator's wallet and are made available to the player's account for gaming use. Otherwise, if the operator receives a transaction from a player's account without first being notified, the funds are sent back to the originating wallet. In this scenario, the operator does not assign an individual wallet to each player. Instead, every player is assigned ownership of a balance virtually segregated within one of the operator's holding wallets; and

(ii) a "multiple wallet system"– in the second scenario, the operator assigns a gaming wallet for each currency to every player's account. The MGA only accepts this case if the operator has an intermediate wallet structure comprised of one or more wallets. Such an intermediate setup is used to accept deposits from the player's personal external source of funds. However, in contrast to that scenario, if the deposited amount is within the "maximum amount", the funds are forwarded to the player's respective VC gaming wallet rather than allocating players a share of the operator's wallet. The intermediate wallet reverses incoming transactions if they exceed the "maximum amount" and/or if the funds come from a wallet that is not expected to make a deposit. The player uses the account with the operator to inform of an incoming deposit and get feedback from the operator of the deposit being awaited.

More recently, in June 2018, the Malta Stock Exchange announced its MSX Fintech Accelerator, an initiative endorsed by Binance and Thomson Reuters, which is an accelerator providing a programme designed to mentor and support start-ups and entrepreneurs in the crypto and blockchain space, matching them with international technology and business leaders.

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From a broader perspective, Malta has also experienced a flurry of collaborative activity amongst various stakeholders, with a variety of associations and interest groups being formally established to further the development of the cryptocurrency community in Malta, sharing the common goal of providing a mutual educational and learning experience and fostering a business environment that is conducive to these innovations. Examples include:

- BitMalta;
- the Blockchain Malta Association;
- the Blockchain Research Group, University of Malta; and
- the Malta Information Technology Agency (MITA) – YouStartIT Accelerator.

Finally, in April 2018, Malta joined another 23 European Union Member States in establishing the European Blockchain Partnership ("**EBP**"). The EBP is intended to act as a vehicle for co-operation among 23 EU Member States in terms of exchanging experience and know-how in technical and regulatory fields.

Ownership and licensing requirements

Owning cryptocurrencies for investment management purposes

As set out above, according to the provisions of the VFAA, a licensing requirement is triggered under the VFAA where an entity provides a service set out in the second schedule of the VFAA in relation to a VFA, whether such services are provided in or from within Malta (note that the VFAA does not define the phrase '*in or from within Malta*'; however, we interpret this to mean: (i) the provision of a VFA service by an entity from within Malta; or (ii) the provision of services by an entity to clients in Malta on a cross-border basis).

Investment management is one of the services listed in the second schedule to the VFAA. Accordingly, where such service is provided in respect of VFAs in or from Malta, this would trigger a licensing requirement under the VFAA and such person would be required to obtain a licence under the VFAA to carry out this activity.

Please note that according to draft legislation (which has yet to be implemented) (the "**Draft Legislation**"), exemptions are available where the investment manager manages the investments for its own account (that is, on a proprietary basis) and does not: (i) receive, directly or indirectly, any remuneration or other benefit for the service; (ii) hold himself out as providing a VFA service; or (iii) solicit members of the public to take such services.

Licensing requirements for advisors and fund managers

Investment advice

Investment advice is also listed in the second schedule to the VFAA. Accordingly, a licensing requirement would be triggered under the VFAA where such service is provided in relation to one or more VFAs in or from Malta.

Fund management

As a preliminary matter, please note that, in terms of Maltese law, it is possible for a Maltese domiciled fund to be structured as: (i) a UCITS fund; (ii) an alternative investment fund ("**AIF**"); or (iii) a professional investor fund ("**PIF**"). At the time of writing, Maltese domiciled AIFs and UCITS are not permitted to invest in cryptocurrencies. Therefore, it is currently only possible for Malta-domiciled collective investment schemes to invest in cryptocurrencies when structured as PIFs (which are subset of AIFs available to managers

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which fall within the *de minimis* thresholds set out in the AIFMD (Directive 2011/61/EU)).

The licensing requirements for the management of a Malta-domiciled PIF will depend on whether the management company is established in or outside Malta.

Fund managers which manage PIFs investing in cryptocurrencies through a management company established in Malta are required to be licensed under the Investment Services Act (Chapter 370 of the Laws of Malta, the "**ISA**"). In line with the Draft Legislation, such fund manager would not require a separate licence under the VFAA to manage a PIF investing in cryptocurrencies.

Fund managers which manage PIFs investing in cryptocurrencies through a management company established outside Malta are not required to be licensed under the ISA. However, in order for the foreign-based entity to manage the PIF, the MFSA must be satisfied that such management company has the necessary skills, competence and expertise to manage the PIF. A fund manager domiciled overseas which is managing a Malta-domiciled PIF would not require a separate licence under the VFAA.

Mining

Cryptocurrency mining activities are permitted but are, at the time of writing, unregulated.

Border restrictions and declaration

At the time of writing, there are no border restrictions or obligations to declare cryptocurrency holdings.

Reporting requirements

As at the time of writing, there are no reporting requirements for cryptocurrency payments made in excess of a certain value.

Estate planning and testamentary succession

As at the date of writing, there are no laws regulating the treatment of cryptocurrencies for the purposes of estate planning and testamentary succession; general laws such as the relevant provisions found within the Civil Code (Chapter 16 of the Laws of Malta) would apply.

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Malcolm Falzon is the partner at Camilleri Preziosi responsible for the firm's insurance, gaming and aviation practices. His areas of specialisation also comprise corporate and M&A, capital markets, securitisation, asset finance and pensions. He regularly advises local and international clients on legal, regulatory, operational and licensing matters as well as related corporate and commercial and dispute resolution issues across various industry sectors. Malcolm also leads Camilleri Preziosi's Blockchain Taskforce, which was set up in order to study the technology and its potential application to the industry sectors serviced by the firm. He regularly acts as an examiner at the University of Malta and lecturer at the Malta Stock Exchange Institute, and is a speaker at seminars and conferences relating to his areas of expertise. Following his traineeship at the firm and return from postgraduate studies at University College, London, Malcolm returned to the firm as an associate in 2005, and was admitted to partnership in 2013.

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Alexia forms part of Camilleri Preziosi's Technology, Media and Telecoms department and the firm's Blockchain Taskforce. Her areas of specialisation include fintech regulation, technology, intellectual property and data protection. She often works on DLT-related matters, specifically within the field of cryptocurrencies, initial coin offerings and related services. Her interests lie in the development of nascent technologies such as artificial intelligence and the internet of things, and the legal implications which arise as a result of their development. She frequently contributes to Camilleri Preziosi's publications on the applicability of these technologies to various industry sectors. She also regularly assists clients with data protection and intellectual property-related matters. Alexia graduated from The City Law School in London in 2016 after completing the Graduate Diploma in Law course. Prior to this, Alexia obtained a First-class Honours degree in Pharmacology from the University of Portsmouth in 2015.

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