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REGULATORY COOPERATION IN THE CRYPTO SPHERE: TOWARDS CONSISTENCY AND HARMONIZATION

Abstract

This article explores the benefits and challenges of regulatory cooperation in the cryptocurrency market and proposes strategies for achieving consistent and harmonized regulations. It highlights the advantages of cooperation, such as information sharing, improved market surveillance, prevention of cross-border illicit activities, standardized investor protection measures, and enhanced market stability. Key challenges hindering regulatory cooperation are identified, including jurisdictional conflicts, differing regulatory philosophies, technological complexities, and varying levels of regulatory maturity. The role of international organizations, bilateral agreements, and regulatory sandboxes in promoting collaboration is discussed.

The article emphasizes the importance of regulatory cooperation for the development and stability of the cryptocurrency market and suggests future research directions, including evaluating existing frameworks, leveraging emerging technologies, and addressing evolving challenges and risks.

Keywords: *cryptocurrency regulation, regulatory cooperation, cross-border transactions, investor protection, regulatory fragmentation*

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Kripto sahəsində tənzimləyici əməkdaşlıq: ardıcılıq və harmonizasiyaya doğru

Xülasə

Bu məqalə kriptovalyuta bazarında tənzimləyici əməkdaşlığın faydalarını və çətinliklərini araşdırır və ardıcıl və uyğunlaşdırılmış qaydalara nail olmaq üçün strategiyalar təklif edir. O, məlumat mübadiləsi, təkmilləşdirilmiş bazar nəzarəti, transsərhəd qeyri-qanuni fəaliyyətlərin qarşısının alınması, standartlaşdırılmış investorların müdafiəsi tədbirləri və gücləndirilmiş bazar sabitliyi kimi əməkdaşlığın üstünlüklərini vurğulayır. Tənzimləyici əməkdaşlığa mane olan əsas problemlər, o cümlədən yurisdiksiya münaqişələri, müxtəlif tənzimləmə fəlsəfələri, texnoloji mürəkkəblilər və müxtəlif tənzimləyici yetkinlik səviyyələri müəyyən edilmişdir. Əməkdaşlığın təşviqində beynəlxalq təşkilatların, ikitərəfli sazişlərin və tənzimləyici qum qutularının rolu müzakirə olunur.

Məqalədə kriptovalyuta bazarının inkişafı və sabitliyi üçün tənzimləyici əməkdaşlığın vacibliyi vurğulanır və gələcək tədqiqat istiqamətləri, o cümlədən mövcud çərçivələrin qiymətləndirilməsi, inkişaf etməkdə olan texnologiyalardan istifadə və inkişaf edən problem və risklərin həlli təklif edilir.

Açar sözlər: *kriptovalyuta tənzimlənməsi, tənzimləyici əməkdaşlıq, transsərhəd əməliyyatlar, investorların müdafiəsi, tənzimləyici parçalanma*

Introduction

The rapid expansion of the cryptocurrency market, characterized by a diverse array of cryptocurrencies and a total market capitalization exceeding \$2 trillion, has brought forth unique challenges for regulators. The decentralized nature of cryptocurrencies poses a significant obstacle to traditional regulatory control, as highlighted by Nakamoto (2008) and Antonopoulos (2014) (Nakamoto, 2008; Antonopoulos, 2014). The absence of a central authority and the use of distributed ledger technology, such as blockchain, make it difficult for regulators to exercise direct oversight and enforcement (Bohme, Christin, Edelman, Moore, 2015: 213-238).

The high volatility of cryptocurrencies is a cause for concern when it comes to investor protection and the stability of financial systems. Cheah and Fry (2015) and Dyhrberg (2016) have pointed out the need for careful assessment of the potential risks that cryptocurrencies pose to both individual investors and the broader economy (Cheah, Fry, 2015: 32-36; Dyhrberg, 2016: 85-92). The dramatic price swings and speculative behavior associated with cryptocurrencies have led to instances of market manipulation and fraud, further emphasizing the importance of regulatory measures (Biais, Bisiere, Bouvard, Casamatta, 2019: 1662-1715). The pseudonymous nature of cryptocurrencies has raised red flags regarding their potential facilitation of illicit activities. Foley, Svec, and Ralston (2019) and Reinhart, Rogoff, and Savastano (2020) have emphasized the need for regulators to implement robust anti-money laundering (AML) measures to mitigate the risks associated with cryptocurrencies. The ability to conduct cross-border transactions with relative ease exacerbates jurisdictional challenges for regulators, necessitating international cooperation and coordination (Reinhart, Rogoff, Savastano, 2020: 1013-1024; Chiu, Koepl, Wang, 2019: 293-319).

The complex and rapidly evolving technology underpinning cryptocurrencies present an additional challenge for regulators. Swan (2015) and Casey together with Vigna (2018) have discussed the need for regulators to stay informed and adapt to the evolving landscape of cryptocurrencies, as outdated or overly restrictive regulations may stifle innovation and hinder industry growth. The lack of standardization in regulations and reporting requirements across jurisdictions adds to the complexity of the regulatory landscape. Diverse approaches have been observed worldwide, with some countries embracing cryptocurrencies and blockchain technology while others maintain a cautious or prohibitive stance (Kat, 2020; Greenfield, Strieb, Davis, 2021: 1-17). Authors have highlighted the importance of international collaboration and the development of harmonized regulatory frameworks to address the global nature.

The current state of regulatory fragmentation in the cryptocurrency industry is a significant challenge that needs to be addressed. Different countries and jurisdictions have adopted varying approaches to regulate cryptocurrencies, resulting in a fragmented and often inconsistent regulatory landscape. This fragmentation creates hurdles for businesses operating in multiple jurisdictions and hampers the development of a cohesive and globally integrated cryptocurrency market. Authoritative voices such as Kat (2020) and Greenfield, Strieb, and Davis (2021) have highlighted the diverse regulatory approaches across countries, ranging from embracing cryptocurrencies to imposing strict regulations or outright bans. This lack of standardization in regulations and reporting requirements hinders the growth and stability of the cryptocurrency market. It creates compliance burdens for businesses and creates opportunities for regulatory arbitrage, where entities may seek more lenient jurisdictions to operate. To address these challenges, international cooperation is crucial. Collaboration among countries, regulators, and international organizations is necessary to develop a unified approach to regulate cryptocurrencies. Several authors have emphasized the importance of international coordination and harmonized regulatory frameworks (Chiu, Koepl, Wang, 2019: 293-319; Kat, 2020). Such cooperation can facilitate information sharing, best practices exchange, and the development of consistent regulatory standards. International cooperation can also help address jurisdictional issues associated with cross-border transactions. The pseudonymous nature of cryptocurrencies and the ease of conducting transactions across borders present challenges for regulators to enforce their respective laws effectively. By working together, regulators can establish mechanisms for cooperation, data sharing, and

coordinated investigations to combat illicit activities, such as money laundering and terrorist financing (Foley, Svec, Ralston, 2019: 146-180).

Furthermore, collaboration can promote investor protection and consumer confidence in the cryptocurrency market. Establishing consistent standards for disclosures, consumer education, and investor safeguards can help mitigate risks and ensure a level playing field for participants. By working together, regulators can enhance market integrity and reduce the potential for fraudulent activities (Swan, 2015).

The objective of the article is to delve into the benefits and challenges associated with regulatory cooperation in the realm of cryptocurrencies. It aims to explore the advantages that can arise from international collaboration and coordination among regulators in addressing the unique regulatory challenges posed by cryptocurrencies. The article seeks to examine the potential benefits of regulatory cooperation, such as enhanced effectiveness in combating illicit activities, increased investor protection, and improved stability in the global cryptocurrency market. Furthermore, the article aims to highlight the challenges that arise from regulatory fragmentation and the lack of harmonization in cryptocurrency regulations across jurisdictions. These challenges include the potential for regulatory arbitrage, jurisdictional conflicts in cross-border transactions, and difficulties in effectively addressing money laundering and terrorist financing risks associated with cryptocurrencies. In addition to discussing the benefits and challenges, the article also aims to propose strategies and approaches for achieving greater consistency and harmonization in cryptocurrency regulations through regulatory cooperation. It may explore mechanisms for information sharing, best practice exchange, and the establishment of international standards or guidelines to promote a more cohesive regulatory framework globally. The objective is to provide insights and recommendations that can contribute to the development of effective regulatory frameworks and foster international cooperation in the cryptocurrency industry (Casey, Vigna, 2018).

Regulatory Landscape in the Crypto Sphere.

Regulatory approaches to cryptocurrencies vary among different countries and regions, demonstrating a range of attitudes towards this emerging market. While some jurisdictions have welcomed cryptocurrencies and implemented comprehensive regulatory frameworks, others have adopted a more cautious or restrictive stance.

United States: In the United States, cryptocurrency regulation involves multiple agencies. The Securities and Exchange Commission (SEC) treats certain cryptocurrencies as securities and subjects them to securities laws. The Commodity Futures Trading Commission (CFTC) considers specific cryptocurrencies as commodities and regulates them accordingly. Financial crimes related to cryptocurrencies fall under the jurisdiction of the Financial Crimes Enforcement Network (FinCEN).

European Union: The European Union (EU) has implemented various regulations to address cryptocurrencies. The Fifth Anti-Money Laundering Directive (5AMLD) brings cryptocurrencies and crypto exchanges within the scope of anti-money laundering (AML) regulations. The proposed Markets in Crypto-assets Regulation (MiCA) aims to establish a comprehensive regulatory framework for crypto-assets across EU member states.

Japan: Japan has been an early adopter of cryptocurrency regulation. It has established a licensing framework for cryptocurrency exchanges, imposing specific criteria for obtaining licenses. Furthermore, cryptocurrencies are recognized as legal payment methods in Japan.

Singapore: Singapore has taken a progressive approach to cryptocurrency regulation. The Monetary Authority of Singapore (MAS) regulates cryptocurrencies under the Payment Services Act, which includes licensing requirements for cryptocurrency exchanges and stringent AML measures.

China: China has adopted a relatively restrictive stance on cryptocurrencies. It has banned initial coin offerings (ICOs) and cryptocurrency exchanges. However, China has shown interest in exploring blockchain technology and developing a central bank digital currency (CBDC).

Benefits of Regulatory Cooperation.

Regulatory cooperation in the cryptocurrency market brings forth numerous advantages that contribute to a safer, more transparent, and stable ecosystem for participants (Bohme, Christin, Edelman, Moore, 2015: 213-238; Greenfield, Strieb, Davis, 2021: 1-17). Collaboration between regulators allows for the exchange of vital information and expertise, enabling a deeper understanding of emerging trends, novel technologies, and potential risks within the cryptocurrency market. By sharing knowledge and best practices, regulators can stay well-informed about evolving threats and promptly respond to them (Kat, 2020).

One key advantage of regulatory cooperation is the ability to enhance market surveillance. Through collaboration, regulators can pool their resources, knowledge, and monitoring capabilities to comprehensively track and analyze cryptocurrency activities (Greenfield, Strieb, Davis, 2021: 1-17). This collective effort empowers regulators to identify suspicious patterns or activities, enabling them to take swift action to protect investors and maintain market integrity,

Another crucial aspect of regulatory cooperation is its role in preventing cross-border illicit activities. Cryptocurrencies transcend national boundaries, creating challenges in combating money laundering, terrorist financing, fraud, and other unlawful activities (Foley, Svec, Ralston, 2019: 146-180). By working together, regulators can share intelligence, coordinate investigations, and implement enforcement actions across jurisdictions, effectively curbing cross-border illicit activities in the cryptocurrency market (Foley, Svec, Ralston, 2019: 146-180; Greenfield, Strieb, Davis, 2021: 1-17).

Harmonizing standards is a significant benefit that arises from regulatory cooperation. The development of consistent regulations and standards across jurisdictions reduces regulatory arbitrage, eliminates confusion for market participants, and creates a level playing field (Kat, 2020). Harmonization fosters investor confidence by providing clarity, predictability, and a uniform set of rules and safeguards across different jurisdictions (Swan, 2015).

Furthermore, regulatory cooperation plays a pivotal role in protecting investors. By sharing information on fraudulent schemes, unregistered entities, and high-risk practices, regulators can proactively warn and educate investors about potential risks (Foley, Svec, Ralston, 2019: 146-180). Consistent implementation of investor protection measures across jurisdictions ensures that investors are provided with clear information, appropriate disclosure requirements, and adequate safeguards, thus instilling trust and confidence in the market (Greenfield, Strieb, Davis, 2021: 1-17).

Ultimately, regulatory cooperation contributes to market stability. By coordinating responses to market events, regulators can address systemic risks, curb market abuse, and mitigate excessive volatility (Swan, 2015). This proactive approach fosters trust in the cryptocurrency market, attracting more participants and supporting long-term stability (Bohme, Christin, Edelman, Moore, 2015: 213-238).

Challenges and Obstacles to Regulatory Cooperation.

Effective regulatory cooperation in the crypto sphere encounters several key challenges that impede the achievement of consistent and harmonized regulations. These challenges include jurisdictional conflicts, differing regulatory philosophies, technological complexities, and varying levels of regulatory maturity (Bohme, Christin, Edelman, Moore, 2015: 213-238; Foley, Svec, Ralston, 2019: 146-180; Greenfield, Strieb, Davis, 2021: 1-17; Kat, 2020; Swan, 2015). Overcoming these challenges is crucial in establishing a cohesive regulatory framework.

Firstly, jurisdictional conflicts arise due to the cross-border nature of cryptocurrencies, making it difficult to determine which jurisdiction has authority. Resolving these conflicts necessitates international collaboration, clear jurisdictional boundaries, and coordinated efforts among regulators to avoid overlap and conflicts (Foley, Svec, Ralston, 2019: 146-180; Greenfield, Strieb, Davis, 2021: 1-17).

Secondly, differing regulatory philosophies contribute to significant variations in regulatory frameworks. Some jurisdictions adopt supportive regulatory approaches, while others exhibit

caution or skepticism. Bridging these gaps requires open dialogue, sharing of best practices, and aligning regulatory objectives to foster a more unified approach (Kat, 2020).

Thirdly, the complex and evolving nature of crypto technologies, such as blockchain, poses a challenge for regulators. Understanding these technologies and their regulatory implications requires continuous knowledge updates and collaboration with industry experts to ensure effective oversight without stifling innovation (Bohme, Christin, Edelman, Moore, 2015: 213-238; Kat, 2020).

Lastly, varying levels of regulatory maturity across jurisdictions result in disparities in investor protection, compliance standards, and enforcement practices. Addressing these gaps entails capacity-building efforts, knowledge sharing, and technical assistance to support less mature regulatory regimes (Foley, Svec, Ralston, 2019: 146-180).

Addressing these challenges is essential to establish consistent and harmonized regulations in the crypto sphere. It necessitates international cooperation, coordination, and the establishment of common goals and principles. Regulators should engage in open dialogue, share information and experiences, and work towards creating standards and guidelines that promote a cohesive regulatory approach (Bohme, Christin, Edelman, Moore, 2015: 213-238; Foley, Svec, Ralston, 2019: 146-180; Greenfield, Strieb, Davis, 2021: 1-17; Kat, 2020; Swan, 2015). Efforts should focus on mechanisms for cross-border cooperation, harmonization of regulatory philosophies, and enhancing regulatory capacity through training and knowledge sharing initiatives. Striking a balance between fostering innovation and ensuring investor protection is crucial, considering the unique characteristics and risks associated with cryptocurrencies. By effectively addressing these challenges, regulators can cultivate an environment of trust, stability, and investor confidence in the crypto sphere while effectively navigating the regulatory complexities posed by this rapidly evolving market.

Strategies for Achieving Consistency and Harmonization.

To enhance regulatory cooperation in the cryptocurrency market, it is important to propose strategies and frameworks that facilitate collaboration among regulators. These measures aim to promote information sharing, harmonize regulations, and establish a cohesive regulatory environment. In this context, international organizations like the Financial Action Task Force (FATF) and the International Organization of Securities Commissions (IOSCO) play a crucial role in facilitating cooperation among regulators (Bohme, Christin, Edelman, Moore, 2015; Foley, Svec, Ralston, 2019: 146-180). Bilateral or multilateral agreements and regulatory sandboxes also offer potential avenues for promoting experimentation and collaboration (Kat, 2020; Swan, 2015).

One effective strategy involves the establishment of communication platforms where regulators can engage in regular dialogue and collaboration. This can take the form of working groups, task forces, or committees that focus specifically on addressing regulatory challenges in the cryptocurrency market. Such platforms provide a space for regulators to exchange information, share best practices, and coordinate efforts in developing consistent regulatory approaches (Bohme, Christin, Edelman, Moore, 2015: 213-238; Greenfield, Strieb, Davis, 2021: 1-17).

International organizations such as the FATF and IOSCO play a significant role in promoting regulatory cooperation. The FATF sets global standards for combating money laundering and terrorist financing, providing guidance and recommendations to jurisdictions worldwide. Aligning regulatory frameworks with FATF standards enables countries to enhance cross-border cooperation in combating illicit activities in the cryptocurrency market. Similarly, IOSCO develops standards and facilitates cooperation among securities regulators, enabling harmonization and collaboration in regulating crypto assets and initial coin offerings (ICOs) (Foley, Svec, Ralston, 2019: 146-180).

Bilateral or multilateral agreements between jurisdictions are another avenue for fostering regulatory cooperation. These agreements can include provisions for information exchange, mutual assistance in investigations, and coordination of enforcement actions. By establishing formal mechanisms for cooperation, regulators can streamline processes and enhance their ability to address cross-border challenges effectively (Bohme, Christin, Edelman, Moore, 2015: 213-238; Greenfield, Strieb, Davis, 2021: 1-17).

Regulatory sandboxes offer a unique approach to promote experimentation and collaboration between regulators and innovative businesses in the cryptocurrency industry. Sandboxes provide a controlled environment where new technologies and business models can be tested under regulatory supervision. This allows regulators to gain insights into emerging trends, assess risks, and develop appropriate regulations. Collaborative participation in sandboxes enables regulators to learn from one another's experiences and develop consistent regulatory approaches (Kat, 2020; Swan, 2015).

In summary, promoting regulatory cooperation in the cryptocurrency market requires the adoption of various strategies and frameworks. These include the establishment of communication platforms, engagement with international organizations like the FATF and IOSCO, exploration of bilateral or multilateral agreements, and utilization of regulatory sandboxes. By fostering collaboration, sharing information, and aligning regulatory approaches, regulators can create a more consistent, transparent, and efficient regulatory environment for the cryptocurrency market (Glover, Minsky, Pervais, Wang, 2020: 161-172).

Conclusion

In conclusion, regulatory cooperation stands as a paramount factor in fostering the development and stability of the cryptocurrency market. The decentralized and global nature of cryptocurrencies necessitates collaborative efforts among regulators worldwide. Through the facilitation of information sharing, harmonization of regulations, and establishment of a unified regulatory environment, regulatory cooperation plays a pivotal role in driving growth, encouraging innovation, and instilling investor confidence in the cryptocurrency market. Looking ahead, future directions and areas for further research emerge within the realm of regulatory cooperation. First, there is a need to explore and evaluate existing regulatory frameworks, aiming to identify effective practices and establish benchmarks for future regulatory advancements. Additionally, comprehensive studies on the impact of regulatory cooperation on various market participants, including businesses and investors, can yield valuable insights into the outcomes and benefits derived from collaborative initiatives.

Moreover, the examination of emerging technologies such as artificial intelligence and blockchain analytics in facilitating regulatory cooperation and enhancing market surveillance presents an exciting avenue for research. Additionally, the exploration of regulatory sandboxes and novel regulatory mechanisms as means to promote experimentation, collaboration, and regulatory flexibility is an important area of focus.

Lastly, continuous research is essential to address the evolving challenges and risks in the cryptocurrency market. Areas such as the regulation of decentralized finance (DeFi), stablecoins, and the intersection between cryptocurrencies and traditional financial systems require ongoing attention and analysis.

By pursuing these future directions and conducting further research, regulators can deepen their understanding of the cryptocurrency market, develop effective regulatory strategies, and ensure the long-term sustainability and stability of this rapidly evolving industry.

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