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CRYPTO REAL ESTATE – "NEW COOL KID ON THE BLOCK?"

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The real estate market is constantly evolving and has experienced great change due to the emergence of new technological tools. Among those, cryptocurrencies, possibly the most cutting-edge technological advancement, are most likely to have a substantial impact on the industry in the years to come.

In order to ascertain the potential impact of this development, it is first necessary to have a clear grasp of the meaning of cryptocurrency, namely "what is a cryptocurrency and how is it changing real estate investment?"; "why is it a hot topic?", and "what is the future of this asset class in the industry?"

The answers are neither straightforward nor simple, but one thing is for sure: we are witnessing one of the most significant technological breakthroughs in recent generations.

In a nutshell, cryptocurrencies are a purely peer-to-peer version of electronic money, but which do not in principle have legal tender, which are based on blockchain technology, and which allows for online payments to be made from one party to another without going through a financial institution or any other intermediary.

Based on this, it is clear that the revolutionary nature of these digital assets is not connected to their digital or virtual nature, since the vast majority of payments are already made in this way (just think of the endless number of transactions that are made daily through credit or debit cards), but rather to the fact that they enable decentralization through the exclusion of a third party (such as governments, banks, or other financial institutions) from their traditional role in a financial transaction, thus enabling greater autonomy, confidentiality and cost reduction in such operations.

The initial skepticism towards this asset class has gradually given room to a greater awareness and curiosity over its potential, and nowadays there is no shortage of people with the ambition to apply the capabilities of cryptocurrencies to new market segments.

This increased awareness around cryptocurrencies has allowed for a shift in the way they are perceived: if previously they were seen only as an asset, functioning, therefore, as any other investment, today they are getting closer and closer to the function for which they were initially conceived, i.e., to be an effective means of transaction to acquire any type of goods or services.

It is precisely from the intersection of this new perception of cryptocurrencies and the desire to apply their potential to once neglected areas that crypto real estate has emerged.

In Portugal, the appetite for buying real estate with cryptocurrencies has increased, particularly by foreign investors who see the country as one of the most popular destinations for the crypto community. In fact, Portugal does not tax capital gains from cryptocurrencies holdings, although that is about to change with the proposal for the 2023 Portuguese State Budget which includes capital gains taxation for cryptocurrencies. Notwithstanding, many people recognize the capacity of Portugal to become a crypto hub, so it is not surprising that the urge to buy houses using cryptocurrencies is becoming a more preeminent reality as these seem to be here to stay, regardless of their volatility.

In practice there are two ways of buying real estate with these digital assets. On the one hand, it is possible to carry out such operations by converting cryptocurrencies into fiat money. In this scenario, there is no direct handover of cryptocurrencies to the seller. Instead, the buyer resorts to a broker, who converts, through a financial institution, the cryptocurrencies into fiat currency for the seller. In this context, it is up to the brokerage firm

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to dispel the risks as to the origin of the money, while the notary will continue to proceed with the standard formalities foreseen for the transaction at hand. This is undoubtedly the approach taken by the vast majority of countries, since the lack of resources to assess the tax implications and inherent risks (notably risks connected to money laundering and terrorist financing), , implies that conversion to fiat money is still required at some stage along the way. Also, conversion to fiat locks the value of the cryptocurrency to avoid the risk of its price fluctuation.

On the other hand, it is also feasible to buy real estate directly using cryptocurrencies as a means of payment, i.e., without the need for conversion into fiat currency - and that is what has already occurred in Portugal.

Portugal's first sale purely made through cryptocurrencies took place on May 4th 2022, in Braga. Although the closing of the deal took only a couple of minutes, it was the result of an extensive period of negotiation between several relevant entities, such as financial and tax authorities and notaries, in order to regulate how such transactions should be performed. Contrary to the general panorama prevailing in this field, there was a concerted effort by the aforementioned entities for such discussions to result in clear indications on the manner in which these transactions should be conducted, which ultimately led to an internal regulation of the Order of Notaries comprising tight rules that notaries must follow when performing deeds of purchase and sale of properties in cryptocurrencies. For a thorough understanding of this phenomenon, familiarity with these rules is imperative.

First of all, it is crucial to bear in mind that the deal must be framed as an exchange (permuta), where the real estate is exchanged for another asset, i.e. cryptocurrencies. Furthermore, this kind of transaction should be regarded as a risky deal for the prevention of money laundering and other tax offences, giving rise to a number of reporting obligations placed on the purchasers.

Therefore, those who intend to buy properties with cryptocurrencies will be required to inform the notaries up to five days before the public deed of the following information, which should subsequently be transmitted to the DCIAP (*Departamento Central de Investigação e Ação Penal*) and the Financial Intelligence Unit (*Unidade de Informação Financeira*):

(i) identification of the parties involved in the transaction (name, profession, address);

(ii) price and type of cryptocurrency;

(iii) evidence of the acquisition of the cryptocurrencies used in the deal (notably, records from the purchase of the virtual currencies to the time of the deal);

(iv) information on the wallets of the purchaser and the buyer; and

(v) date of the public deed.

If the transaction is over € 200,000.00, a set of additional rules is also applicable in relation to the prior communications mentioned above, namely the need to communicate the transaction to the authorities and to compare the value of the cryptocurrencies at the execution date of the promissory sale and purchase agreement and their value at the date of the public deed.

This second approach has delighted many crypto-enthusiasts, who put forward as clear advantages the fact that such an option provides for diversification of their portfolios and secure cash-out of cryptocurrencies without loss of value, as well as the fact that it enables direct negotiation between the parties, without having to seek the bank's permission for the execution of bank transfers or cheque issuance.

Yet, this option is only available for those who do not have to resort to taking out a mortgage, as there is still no bank in Portugal authorized to grant mortgages by this means. Additionally, it is important to highlight that in the wider context of purchasing real estate, some payments will still need to be made in fiat currency, particularly those owed to intermediary parties and governmental bodies, such as the direct payment of taxes on real estate transactions or the payment of notary fees.

There is no denying that the Portuguese real estate market, sometimes classified as conservative, is going through one of its most dynamic and exciting phases ever, with increasingly sophisticated players seeking new ways of doing business and for whom it is urgent to provide answers to accommodate their equally increasingly complex needs.

It is in this context that crypto real estate has been positioning itself as a reality between key players in the market and real estate lawyers should be paying close attention to the rise of this new phenomenon.

For sellers, acceptance of this method may mean a boost in the ability to attract a new pool of investors, many of them interested in diversifying their portfolios with more stable assets that are not subject to as much volatility, as is the case with cryptocurrencies.

For law firms, the growth of crypto real estate may bring new challenges, but it may also encompass an opportunity to reconsider their legal viewpoints and approach to client counseling.

Having said all this, it seems fair to conclude that crypto real estate is here to stay. Nonetheless, it is worth noting that we are still at an early stage in the development of this phenomenon and that its widespread implementation by clients and parties is not certain. Even if it does happen, it will take some time before gaining general acceptance from the market, which is known for being conservative and wary of legal uncertainty and a lack of regulation, as well as of the security threats that this kind of technological innovation might pose.

It is still too early to figure out whether crypto real estate is indeed the new cool kid on the block, but it is surely time to assert that it is at least the one to watch. ■