



More Asian regulators to regulate crypto-related activities this year

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Regulating cryptocurrency-related activities look set to top the agenda for many Asian regulators following a slew of proposed measures recently announced in the region's leading financial centres that are leading the pack.

The Hong Kong Securities and Futures Commission (SFC) and the Monetary Authority of Singapore (MAS) have been front-runners in regulating crypto activities, with a number of announcements made in recent months. The Securities Commission Malaysia is the latest regulator to make clear its intention, in an announcement on January 14, to regulate the offering and trading of digital assets.

The SFC has proposed to regulate a number of areas pertaining to crypto activities. Crypto assets will be treated as securities assets and they will be subject to Hong Kong's securities laws. This requires market participants dealing in crypto assets to apply for a Type 1 activity licence. Portfolio or asset managers managing portfolios consisting of crypto assets will be subject to the Type 9 licensing requirements. The SFC will also introduce an opt-in approach to regulate virtual assets trading on electronic platforms.

MAS is also moving one step closer toward regulating crypto exchanges and dealing in crypto assets, following the passage of the Payment Services Bill into law in January, widely expected to be implemented in the second or third quarter this year.

"This is a year of crypto regulations. We are seeing the whole world moving toward regulating crypto-related activities. Regulators are likely to focus on three main areas: crypto trading platform providers, investors investing into crypto assets and asset managers dealing in crypto assets as part of their portfolios," said Kishore Ramakrishnan, co-founder of Temple Grange Partners, a regulatory consultancy in Hong Kong.

The Hong Kong approach

The SFC's approach toward regulating crypto-related activities offers a helpful insight into the direction other regulators will take for such digital assets. Its consultation paper released in December 2018 dealt with the treatment of crypto assets, which is to subject such assets to Hong Kong's securities law. Asset managers in the special administrative region which already hold a Type 9 licence but now manage crypto assets will be required to extend the licence to cover the new crypto activities, according to Ramakrishnan.

Under the SFC's opt-in regime in regulating virtual assets, crypto trading platform providers will be invited to operate in the SFC's regulatory sandbox without a licence for a period of time, during which the SFC will observe and assess the capability and reliability of such platform providers. Once the SFC is convinced of their capability, it will determine, on a case-by-case basis, whether the crypto trading platform providers will be allowed to operate in the public domain, Ramakrishnan said.

Crypto trading platform providers will also be subject to the SFC's enhanced know-your-customer and customer due diligence requirements.

"Trading of cryptocurrencies is typically done on an anonymous basis. As a result, investors are at the risk of dealing with proceeds from money laundering, terrorist financing or drug trafficking. But this will no longer be possible as crypto platform providers in Hong Kong will be subject to enhanced KYC and customer due diligence," Ramakrishnan said.

Recognising that crypto trading platforms are susceptible to significant cyber risk, the SFC is also focusing on investor protection by requiring third-party custodian banks to be set up to safeguard crypto assets.

"Custody is mainly to address investor protection in the event that a crypto exchange goes bankrupt. Crypto exchanges are exposed to cyber risk and operational risk," Ramakrishnan said.

The requirement for third-party custodian banks to be appointed has presented vast opportunities for traditional custodian banks, and a number have begun developing solutions to provide custody for digital assets, according to Ramakrishnan.

Singapore's approach

Market players offering crypto-related activities and potential initial coin offering issuers targeting Singapore-based investors are also watching local regulatory developments closely. MAS' focus on anti-money laundering, rather than consumer protection, in regulating crypto exchanges and dealing in crypto assets has caught the

market's attention.

"This is interesting because this is the first time that MAS is regulating crypto activities. MAS has said that it will amend the definition of crypto activities going forward as the crypto industry is still evolving. I think MAS will be looking at various activities in this space and [will then] decide whether to regulate them in the future," said Nizam Ismail, head of financial services at RHTLaw Taylor Wessing in Singapore.

Nizam pointed out a number of regulatory gaps for cryptocurrency exchanges. It remains unclear at this stage whether they will be regulated under the Payment Services Act in the future. These include product suitability, disclosure obligations by issuers of cryptocurrency, the selling procedure and marketing of cryptocurrency and initial token offerings, custody and collateral management.

There have also been a number of regulatory developments on securities tokens in Singapore. One such development is the amendment of the guidelines on securities tokens. The fast pace at which the crypto industry is moving has led MAS to shorten its approval process for securities token exchanges, termed "recognised market operators" under the guidelines, seeking to operate as such exchanges.

"Recognised market operators are able to go live in the regulatory sandbox upon obtaining MAS' approval, subject to certain volume and transaction constraints. The approval can be obtained within 21 days when the sandbox express regime is in place," Nizam said.

Another development concerns fiat-based stable coins. Under MAS' revised guidelines on securities token where companies are obliged to buy back fiat-based stable coins, they are deemed to have a debt relationship with the investors, and therefore would be deemed to be issuing debentures or securities.

"Questions have been raised about whether fiat-based stable coins will be deemed to be debentures or whether it depends on how they are structured. There is a lot of interest from people waiting to issue stable coins. But if they are structured as securities, it will create regulatory hurdles for [potential] issuers," Nizam said.

There has been speculation MAS may revise the prospectus requirements for issuing initial token offerings.

"My gut feel is that regulators should relook prospectus requirements. A lot of these requirements are overly onerous and may be less relevant in today's context," Nizam said.

Malaysia's approach

The Securities Commission Malaysia has indicated that cryptocurrencies and initial token offerings will be considered as securities, an approach seen as out of sync with the approach taken by regulators in Asian jurisdictions which have begun to regulate crypto-related activities such as Hong Kong, Singapore and Australia.

"In most jurisdictions, they will not treat Bitcoin or Ethereum as securities. In Malaysia, as long as there is an expectation on investment returns, they are considered securities. That is casting a wide net and you could be opening Pandora's box. The analysis seems to be out of sync with what most jurisdictions are doing. Very few jurisdictions treat cryptocurrencies as securities," Nizam said. "The Singapore government, for example, has made it clear that it is not the regulators' job to regulate everything that has an investment element."

- **Patricia Lee** is chief correspondent, banking and securities regulation, Asia