

HONG KONG CRYPTO REGULATION

Webinar 7 - 26 February 2021

GIBRALTAR - DLT REGULATORY FRAMEWORK

- DLT Framework applies to firms that carry on DLT activities i.e. activities that are not subject to regulation under any other regulatory framework that use DLT for the transmission or storage of value belonging to others
- Firms carrying on a business in DLT activities, including crypto trading exchanges and custodians, need to be authorised and licensed as DLT Providers by the GFSC

THE REGULATORY PRINCIPLES

1 | conduct the business with honesty and integrity

2 | pay due regard to customers' interests and needs and customer communication

3 | maintain adequate financial and non-financial resources

4 | effective management and control of the business

5 | effective arrangements in place for the protection of client assets and money

6 | effective corporate governance arrangements in place

7 | systems and security access protocols maintained to appropriate high standards

8 | prevention of financial crime

9 | development of contingency plans for the orderly and solvent wind down of its business

GLOBAL RANKINGS

number of crypto hedge fund managers

1. US
2. UK
3. Gibraltar
4. Hong Kong

AML/CFT REGULATIONS

- Proceeds of Crime Act 2015 amended to extend AML/CFT obligations to undertakings that receive proceeds in any form from the sale of tokenised digital assets whether on their own account or on behalf of another person
- DLT Providers are required to comply with the Proceeds of Crime Act and related guidance issued by the Gibraltar Financial Services Commission
- 5AMLD - brought service providers engaged in exchange services between virtual currencies and fiat currencies as well as custodian wallet providers into the AML/CTF regulatory regime



GIBRLATAR - REGULATION OF ICOs

March 2018 - proposals to regulate ICOs issued

- Proposed regulations would cover the promotion, sale and distribution of crypto tokens, secondary market platforms and investment services relating to tokens conducted in or from Gibraltar
- Virtual assets that fall outside the scope of the DLT Regulations and Gibraltar's financial services and securities laws would be regulated
- Introduction of a requirement for an "authorised sponsor" of all publicly offered ICOs and obligations on authorised sponsors, secondary token market operators and token investment and ancillary service providers

Regulation of the primary market promotion, sale and distribution of tokens that are not securities, outright gifts or donations, extending to activities:

- which purport to be or imply that they are made from Gibraltar;
- are intended to come to the attention of or be accessed by any person in Gibraltar;
- are conducted by overseas subsidiaries of Gibraltar-registered legal persons (in such cases, the Gibraltar person will be liable); or
- are conducted by overseas agents and proxies acting on behalf of Gibraltar-registered legal persons, or on behalf of natural persons ordinarily resident in Gibraltar (in such cases, the Gibraltar person will be liable).



PROMOTION, SALE AND DISTRIBUTION OF TOKENS

DISCLOSURE RULES

require adequate, accurate and balanced disclosure of information to enable anyone considering purchasing tokens in the primary market to make an informed decision

FINANCIAL CRIME PROVISIONS

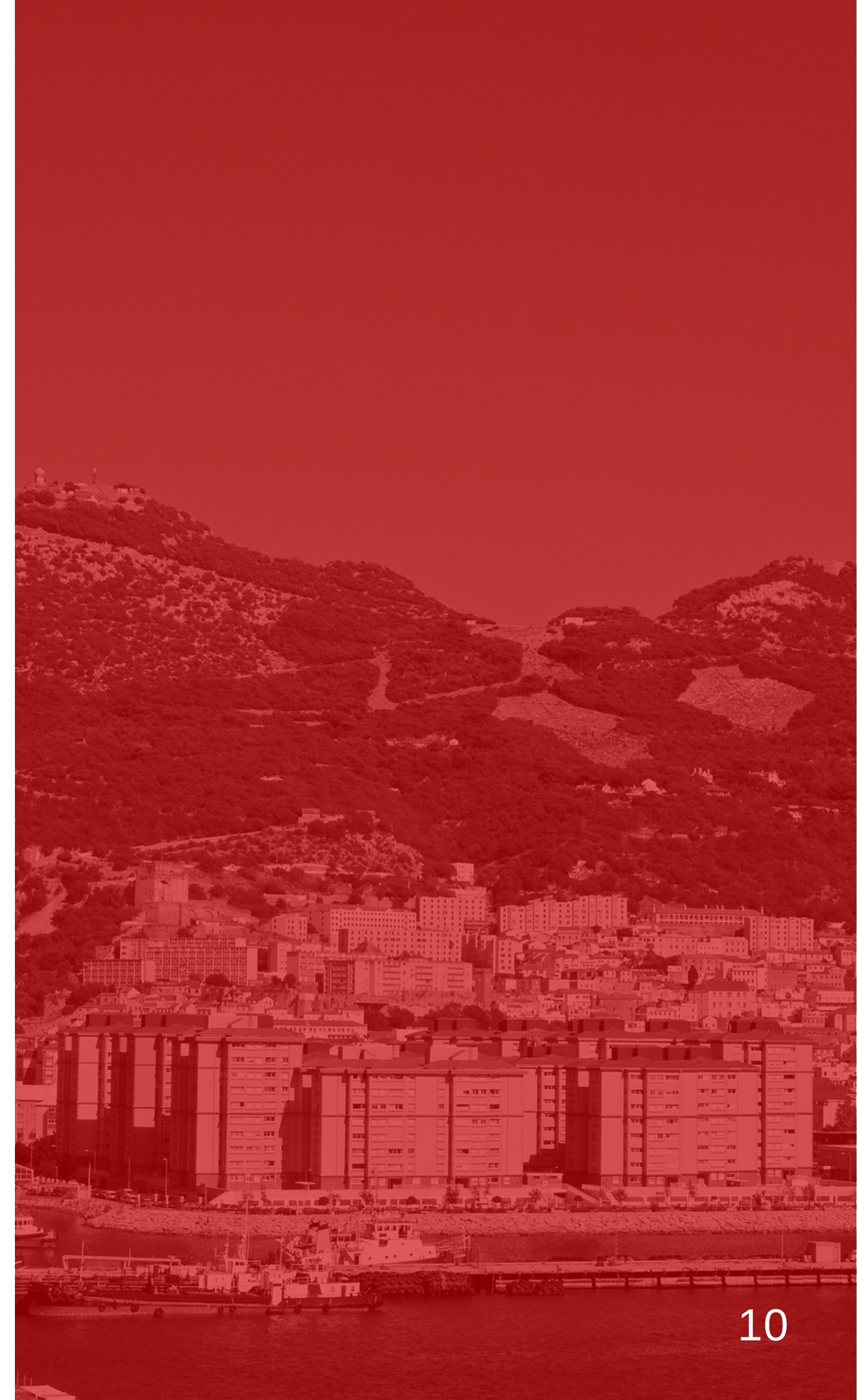
undertakings that receive, whether on their own account or that of another person, proceeds in any form from the sale of tokens are already within the scope of the Proceeds of Crimes Act 2015 (POCA)

AUTHORISED SPONSORS

- An authorised sponsor will need to be appointed in respect of every public token offering promoted, sold or distributed in or from Gibraltar
- Authorised sponsors must have knowledge and experience of ICOs and mind and management in Gibraltar
- Delegation of some of the work will be permitted

CODES OF PRACTICE

- Authorised Sponsors must have in place one or more codes of practice relating to offerings they sponsor
- A code of practice will have to be incorporated in authorised sponsors' agreements with their ICO clients
- Submission of codes of practice will form part of the application process for an authorised sponsor licence
- Prior reporting of amendments to codes of practice will be required and will be treated in the same way as other major business changes
- It is proposed that regulations would specify principles governing the content of codes of practice, however authorised sponsors will be free, subject to approval, to set their own methodologies for implementing the principles



REGISTER OF AUTHORISED SPONSORS

- GFSC will establish and maintain a public register of authorised sponsors and their codes of practice (past and present)
- GFSC will add the following details to the public register:
 - the client(s) for whom they act;
 - the token(s) included in the offering;
 - the code of practice applicable to the offering; and
 - any interest they, and connected persons, have in the tokens offered.

NEW CONTROLLED ACTIVITY AND OFFENCE

It will be an offence to promote, sell or distribute tokens in or from Gibraltar without compliance with:

- the requirement for an authorised sponsor;
- the requirement for a current entry on the public register;
- specified disclosure obligations; and
- relevant provisions of POCA, where applicable.



The proposed regulations will set out requirements for:

- disclosure to the public of data on trading activity;
- disclosure of transaction data to GFSC; and
- specific supervisory actions concerning tokens and positions on token derivatives.



SECONDARY MARKET ACTIVITIES

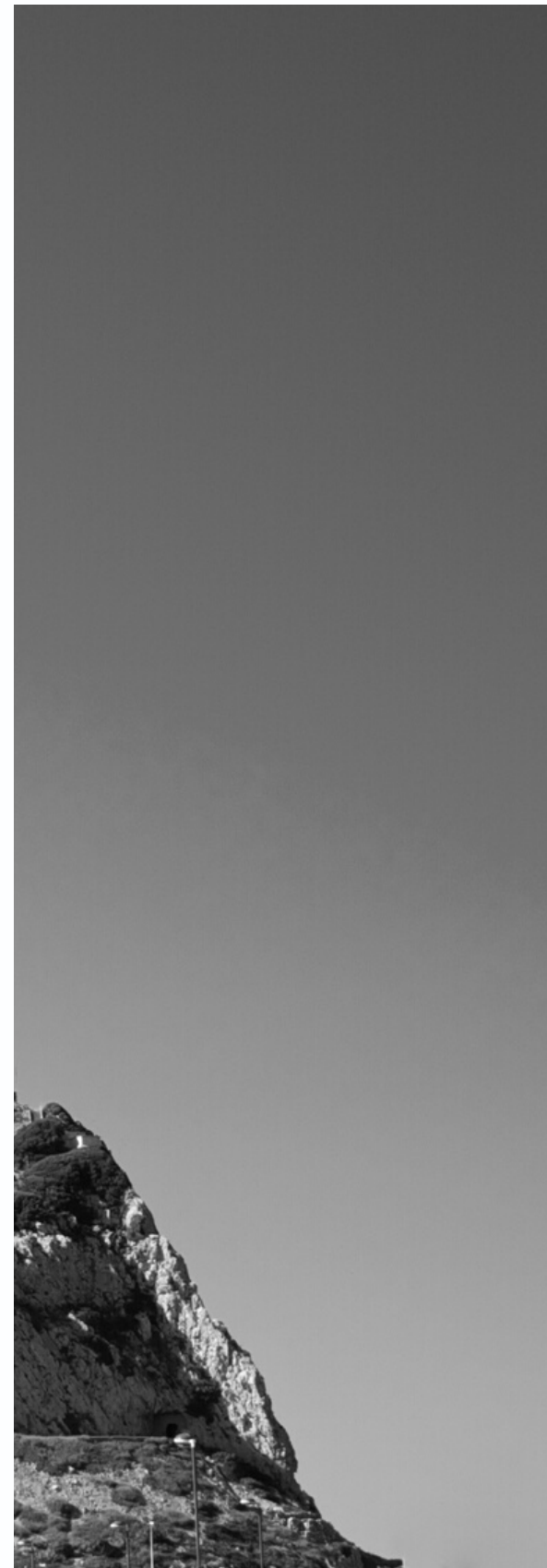
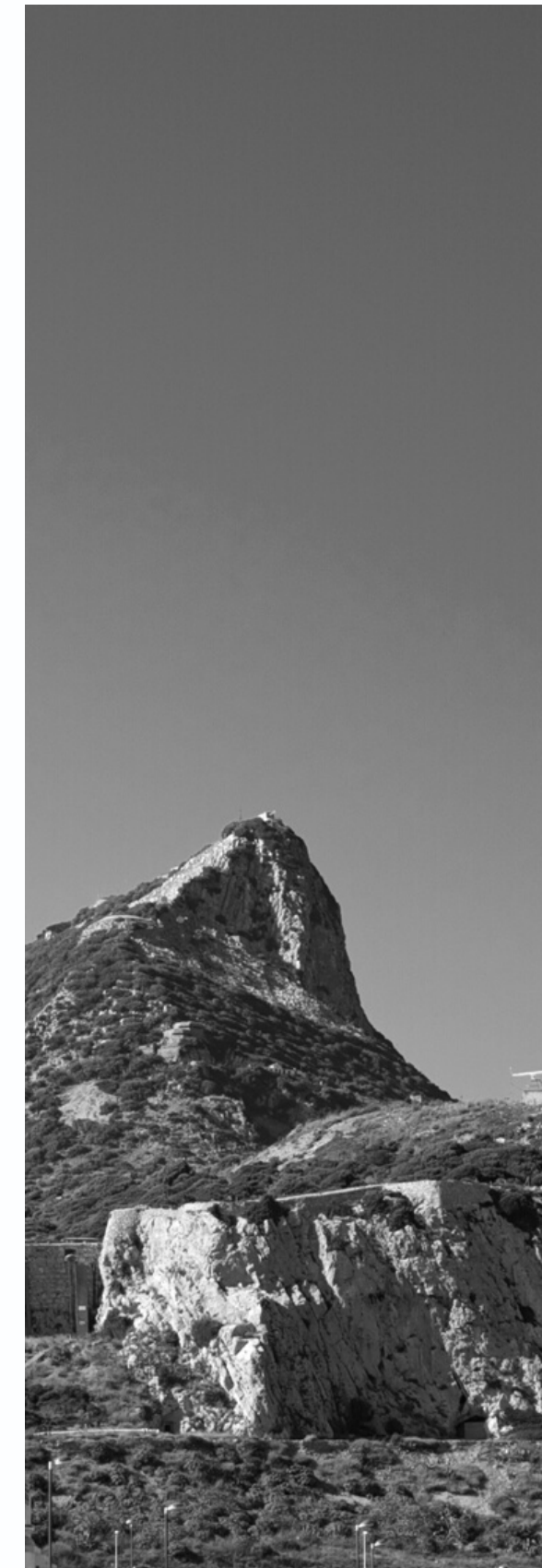
AUTHORISED SECONDARY TOKEN MARKETS

New controlled activity of operating a secondary market platform used for trading tokens and their derivatives

GFSC will authorise and supervise secondary token market operators and maintain a public register of such operators

INVESTMENT AND ANCILLARY TOKEN SERVICES

- generic advice (setting out fairly and in a neutral manner the facts relating to token investments and services);
- product-related advice (setting out in a selective and judgemental manner the advantages and disadvantages of a particular token investment and service); and
- personal recommendation (based on the particular needs and circumstances of the individual investor)



EU PROPOSALS

Which crypto assets will be caught by the regime? - any cryptoassets that are not already subject to EU regulation i.e. utility tokens, stable coins and e-money tokens

"Asset-referenced tokens" - a type of crypto asset that purports to maintain a stable value by referring to the value of several fiat currencies that are legal tender, one of several commodities or one or several crypto assets, or a combination of these assets

"E-money tokens" - crypto assets whose main purpose is use as a means of exchange and that purports to maintain a stable value by referring to the value of a single fiat currency

"Other crypto assets" - intended to cover all other crypto assets which are not covered by other regulatory regimes

EU PROPOSALS (CONT.)

Which crypto asset services will be caught by the regime?

- Trading platform operators, custodial services, and exchange service providers
- The placement of crypto assets, executing payment transactions in asset-referenced tokens and providing advice on crypto assets
- Crypto asset services may only be provided by a legal person with a registered office in an EU Member State and that legal person would have to be authorised and licensed in an EU/EEA Member State as a crypto asset service provider



Issuers of crypto assets - *"any legal person who offers to the public any type of crypto assets or seeks the admission of crypto assets to a trading platform for crypto assets"*

Requirements imposed on issuers:

- (i) must be a legal entity;
- (ii) subject to minimum disclosure requirements and comply with requirement that disclosures are fair, clear and misleading;
- (iii) issuers of asset-referenced tokens must obtain authorisation;
- (iv) must comply with the requirements set out in Article 13 of the MiCA

**EU PROPOSALS
(CONT.)**

EU PROPOSALS (CONT.)

Requirements imposed on issuers of asset-referenced tokens or e-money tokens:

- must be established in the EU
- issuers of e-money tokens must be authorised as an e-money issuer under the E-money Directive
- issuers of stablecoins must be authorised under the MiCA

Exemptions are available from the authorisation requirements for both e-money token issuers and asset-referenced token issuers for small-scale offerings of up to EUR 5 million within 12 months and offerings solely to qualified investors

EU PROPOSALS (CONT.)

"Significant" asset-referenced tokens and "significant" e-money tokens

- Subject to a higher capital requirement of up to 3% of reserve assets and will have to put in place a liquidity management policy
- Assessment of whether a particular token is significant will be made by the European Banking Authority having regard to factors such as a market capitalisation or value of at least EUR 1 billion, having at least 2 million customers and use in at least seven EU member states.



TERRITORIAL APPLICATION

- MiCA would apply across the EU to all member states and would be directly applicable
- Firms outside the EU would be impacted, to the extent that they do business within the EU
- Issuers seeking to issue stablecoins or e-money tokens in the EU would therefore be required to be established in the EU and be duly authorised

COMPARISON AND IMPACT OF EU PROPOSALS

EU

- No overarching regulatory regime
- Handful of EU nations have developed innovative frameworks
- Key benefit of proposals is access to a new EU single market for crypto assets
- Concerns that EU proposals favour incumbent financial institutions

APAC

- Patchwork of regulatory approaches
- Main challenges faced by crypto businesses is understanding and complying with the various requirements and obligations
- Concerns that FSTB proposals will stifle innovation and negatively impact financial inclusion

20%

increase in overall revenue forecast

US\$2 bn

in earnings from PayPal's bitcoin business
alone by 2023

3x as many

bitcoin traders using the app compared to
non-bitcoin users



DBS DIGITAL EXCHANGE

- 10 DEC 2020 - DBS announced it would be setting up the DBS Digital Exchange
- Follows DBS' receipt of in-principle approval by Singapore's MAS recognising the DBS Digital Exchange as a Recognised Market Operator
- Will provide a regulated platform for the issuance and trading of digital tokens back by financial assets; cryptocurrency trading and exchange services between four fiat currencies (including HKD) and four of the “most established” cryptocurrencies and digital custody services
- Will only offer services to institutional investors and accredited investors



BITCOIN FUNDS AND INSTITUTIONAL INVESTMENT

- 20 Jan 2021 - BlackRock reportedly looking at giving two funds the "go-ahead" to invest in bitcoin futures
- 21 Jan 2021 - eToro report found more asset managers are looking at crypto as an asset class