Cryptocurrency and digital assets

A global guide to getting regulated

April 2022

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Introduction

It seems that nothing can slow the pace of innovation unleashed by cryptocurrencies and distributed ledger technology. A global pandemic, tragic events in eastern Europe, and even the ongoing rollercoaster ride of the Bitcoin price have done little to temper the wave of creativity in this frontier market.

With new concepts emerging and gaining acceptance, we all need to expand our lexicon to accommodate terms such as stablecoin, DeFi and NFT. This challenge is particularly acute for regulators, who struggle to keep pace as these innovative ideas increasingly encroach on the existing regulated sphere.

Some of these concepts will be truly disruptive to existing financial markets and financial services businesses, perhaps even replacing concepts that just five or 10 years ago seemed unshakeable. Other innovations may wither on the vine, though it's too early to say which. What's clear is that regulation will be an important determinant of innovative firms' ability to achieve their goals as regulators seek to establish protective measures comparable with those that exist for traditional asset classes.

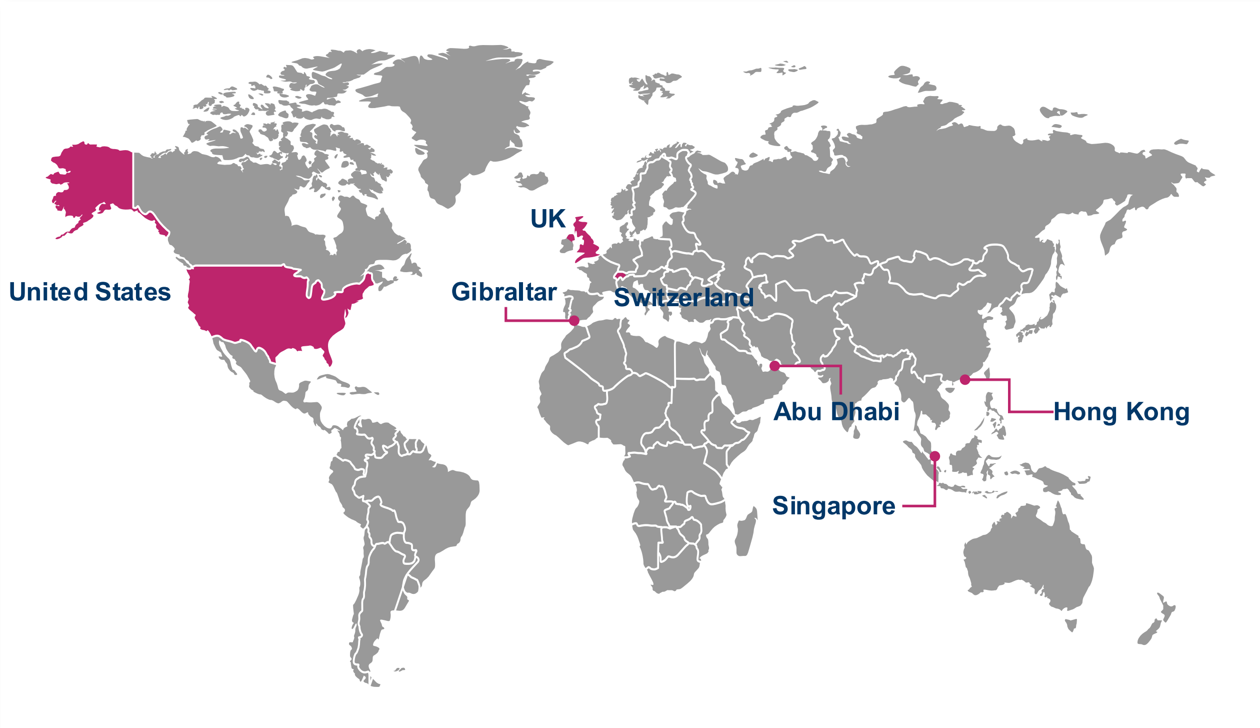
When Bovill first started engaging with cryptocurrency businesses, the burning question for firms was often whether to be regulated or not. Some businesses chose locations where they could be entirely free of regulation, but a growing number sought the credibility conferred by regulated status, even if it meant locating outside major centres for global financial services.

With regulation becoming ever more pervasive, the question for senior leaders in the sector is not so much whether to be regulated, but where. While firms seek out locations with the most efficient regulatory regimes, identifying them means evaluating an array of factors including the scope of regulation and even the sentiment of the regulator in question, as well as ease of access to client groups.

This paper is pitched at senior management teams of cryptocurrency and digital assets businesses, who may have to make decisions regarding which offers to launch where. To inform these decisions, it gives readers an overview of current trends in some key jurisdictions for the industry; complementing our ongoing advice to the sector, which supports growing and internationally minded businesses as they grapple with the complex and evolving regulatory picture.

Damon Batten
Practice Lead, Capital Markets

Summary of major jurisdictions



Territory	Ease of access	Levels of scrutiny	International recognition	Key considerations
United Kingdom	More suitable for those with established products than for relative newcomers due to assessment times and dual application process	Rigorous – requires a robust dual application covering multiple facets	FCA authorisation carries weight globally	A Dual application process with additional fees and time implications to factor in
Singapore	Regulator is keen to grow this sector but with a cautious approach	Rigorous application process with a focus on financial crime prevention and technology risk management	Highly regarded, MAS licence carries weight globally	Ongoing focus on investor protection, financial crime controls and technology risk management

Territory	Ease of access	Levels of scrutiny	International recognition	Key considerations
Hong Kong	An early adopter of Virtual Asset Service Providers – as their approach matures, levels of scrutiny are increasing	Regulation has focused on securities-related assets but is now being expanded	Established regulator whose licenses carry global weight	Firms should be targeting professional investors only Keen focus on investor protection and promotion of investor education
United States	Can be a challenging market to enter to a historic lack of consensus between bodies and each state having differing approaches to regulation	Regulatory situation confusing with multiple regulators and states	Sets the global benchmark for financial services	Use of the 'Howey Test' to identify what your potential regulatory obligations may be
Abu Dhabi	Growing sector with a regulator keen to onboard innovation	Dedicated free market zone which allows targeted focus on helping innovative firms to grow	Emerging credible financial market in the Middle East	Islamic financing laws may apply
Gibraltar	With generally lower application volumes, access may be more streamlined than larger jurisdictions	Rigorous pre-application process with targeted pre application assessment protocols	Attractive environment ranking highly e.g. regarding the number of crypto hedge funds	Passporting capabilities into the UK market allowing for dual market access under one license
Switzerland	Dedicated licensing Act which provides transparency for firms seeking market access	Rigorous application process with clearly defined requirements	Highly regarded with a regulator keen to explore the sector	The 'travel rule' block for transactions conducted on DLT

United Kingdom

For some time, the United Kingdom has positioned itself on the global stage as one of the frontrunners in innovative and alternative finance. From new property lending opportunities to peer-to-peer models, it's often in the UK that innovative businesses first emerge.

Another attraction of the UK is that public sentiment around cryptographic products has seen a positive shift. Research in 2021 showed that nearly 80% of UK adults now recognise what cryptoassets are. True, 38% see purchasing them as a gamble, but this represents a nine percentage point decrease since the previous year, indicating that the asset type is increasingly viewed as a viable investment option. A study by Fidelity later in 2021 found 56% of institutional investors are currently invested in digital assets, compared with 45% in the previous year.

The UK regulator, the Financial Conduct Authority (FCA), is beginning to take note of the increase in demand for digital assets. After a slow start to registration of crypto-related firms, the FCA now seems to be focusing on opening the gates to this new sector. In 2021, Fidelity obtained registration under 5MLD (see below) for a new digital assets entity that will act as a custodian for digital products. This is one of the first examples of a large institution within the financial services sector beginning to offer this service to clients.

24%

annual growth
of institutional investors

Specific considerations

FCA sandbox

The FCA's sandbox initiative has won global respect with their semi-authorisation process allowing innovative firms to test their products in a controlled, cost-effective manner. That is to say that the offering will be tested in a limited and safe environment under the direction of the FCA. The benefit of this approach is that innovative firms in the digital asset space can test new market products in a suitable environment without concern for full regulatory scrutiny – a considerable benefit for early-stage firms, who may not be operationally ready to deliver a full product offering.

We have also observed that sandbox firms have greater success raising funds with investors, as they are able to better showcase their product operating under regulatory scrutiny.

Dual applications

If you wish to offer services involving digital assets, it's likely that you will need to apply for both Part 4A Authorisation and 5MLD registration. The Part 4A application will be required should you look to offer a securitised or tokenised version of a particular asset.

For example, if the digital asset on offer confers rights such as ownership, repayments, or entitlement in future profits, then it is likely to be classified as a Specified Investment under the Regulated Activities Order (RAO). Similarly, a firm engaged in any cryptoasset business – whether with regulated or unregulated tokens – needs 5MLD registration to comply with the Money Laundering Directives introduced in January 2020.

Firms should consider the additional time and cost that both applications are likely to incur. FCA application fees went up in January 2022, with 5MLD registration increasing from £5,000 to £10,000 per application. Ideally, a firm will submit the two applications concurrently to minimise delays.

Ensuring Your Application is Right

It's important that your application is robust at the point of submission: the FCA has authorised very few digital asset firms over the past few years. When developing your application, you should pay particular attention to the following:

Clarity	Be absolutely clear to the FCA (and in particular to the Case Officer) about what you intend to offer. This may sound obvious, but digital assets are still an emerging technology, so clarity around how the product fits into your overall client offering is paramount to ensure the application is assessed correctly.
Financial crime prevention/anti-money laundering (AML)	The FCA will probably pay particular attention to your financial crime prevention and AML methods, as this is one of its biggest concerns. Clearly explain how you will monitor for evidence of financial crime, assess that evidence and escalate matters as required. Document this topic within your financial crime or AML policies.
Investor protection	As a regulated firm, you owe a duty of protection to your customers. Digital asset providers should adopt processes that demonstrate to the FCA how this protection is provided. For example, if you're providing broker services, it's important to have in place a robust best execution process to guarantee the optimum price for digital assets.
Third party engagements	Clear third-party arrangements are essential for firms offering services involving digital assets: an area that's often difficult to police because of the anonymity around blockchain. Whether you're looking at allowing new issuers onto your platforms or dealing with wallet or liquidity providers, you can evidence your legitimacy within the sector by engaging only with trusted firms.

The UK has a lot to offer new Firm's in the digital asset space. Robust regulatory requirements can enable those astute enough to gain Authorisation to flourish on a global scale. Authorisation from the FCA carries global weight, which may be more suitable for firms who are eager to expand their offering more quickly then a firm seeking a jurisdiction to nurture and grow within for the first 5 years.

Singapore

The Monetary Authority of Singapore (MAS) is generally known to adopt a more cautious approach. This is especially true when it comes to cryptocurrencies as an investment asset for retail investors, since their prices are not anchored to any economic fundamentals and are subject to sharp speculative swings; this makes them unsuitable as a medium of exchange, a store of value, or a unit of account. Nevertheless, the MAS takes the view that crypto tokens can bring many potential benefits such as facilitating cheaper, faster cross-border payments and trade finance.

The MAS prefers to call cryptocurrencies by the more technically accurate name - crypto tokens, or digital payment tokens (DPTs) when they are used for payment purposes. DPT services are regulated under the Payment Services Act (PS Act), which is administered by the MAS. Any firm providing DPT services is required to hold a licence under the PS Act unless it qualifies for exemption as specified by Section 13 of the Act.

Under the current definition, a DPT service can be any dealing in DPTs or any facilitation of their exchange where the service provider comes into possession of moneys or DPTs. Amendments expected to take effect later in 2022 will expand the definition to include the transfer or provision of custodian wallet services, as well as facilitation of the exchange of DPTs where the service provider does not take possession of the moneys or DPTs.

From the perspective of AML and countering the financing of terrorism (CFT), DPTs pose higher risks than other assets, given the speed, anonymity, and cross-border nature of the transactions they facilitate. The MAS has stepped up its efforts to set clear supervisory expectations of AML/CFT controls and enhance surveillance of the sector.

Turning to digital assets not being used for payments, under the Securities and Futures Act the MAS regulate any firm that facilitates the offer or issue of digital tokens that are capital markets products, or any firm that facilitates deals involving these tokens. Capital markets products include securities, units in a collective investment scheme, derivatives contracts and leveraged foreign exchange trading. Firms liable to this kind of regulation are subject to similar licensing requirements and regulations to those in place for dealing in traditional capital markets products (i.e., non-digital ones).

The regulator’s central aim, and the focus of the regulatory framework, is to safeguard the reputation of Singapore as a global financial centre, protect consumers, and minimise the risk of DPT service providers being exploited by criminals to launder or hide illicit proceeds. The regulator therefore acts prudently and cautiously in licensing DPT services and sets a high standard for applicants to meet.

Specific considerations

Before choosing Singapore as the home for your DPT services business, it's advisable to take note of the following requirements.

Timelines for approval

The MAS will probably take around a year to approve a licence application, since applications are numerous. Up to March 2022, licences had only been granted to four firms:

- Triple A Technologies Pte Ltd
- DBS Vickers Securities Pte Ltd
- FOMO Pay Pte Ltd
- Independent Reserve SG Pte Ltd

Capital requirements

There are two types of licence – a Major Payment Institution (MPI) licence and a Standard Payment Institution (SPI) licence. You should apply for an MPI licence if you envisage that the total value of all payment transactions that you accept, process, or execute in one month will exceed S$3m (or the equivalent in a foreign currency).

The base capital requirements for MPIs and SPIs are S$250,000 and S$100,000 respectively. MPIs are required to lodge a security deposit with the MAS: S$100,000 if the total value of all monthly payment transactions does not exceed S$6m, or S$200,000 if it does.

AML/CFT controls and technology risk management

Money laundering and terrorism financing are among the MAS's biggest concerns, with many applications being rejected due to weak AML/CFT policies or poor controls. Your policies and procedures in these areas must be strong enough to satisfy the regulator. You should also be able to demonstrate that the policies have been implemented effectively, adequately mitigating money laundering and terrorism finance risks.

Another key concern is technology risk management, particularly the safeguarding of a customer's digital tokens from theft, alongside protection of customer data, transactions, and systems. You must perform a penetration test of your online services, remediate all significant risks identified, and obtain independent validation of the effectiveness of the remediation actions. These steps need to be completed before a licence is granted, though not necessarily before submission of an application.

Competence of directors

Your executive directors and CEO must have sufficient experience in operating a business in the payment services industry or relevant areas of the financial services industry. Individuals managing a large team should also have the relevant experience, competencies, and influence to allow them to exercise effective oversight and control over business activities and staff.

You also need to appoint a suitably qualified compliance officer at management level: an individual with sufficient expertise and authority to oversee your compliance function.

Hong Kong

Hong Kong's virtual asset (VA) market has seen a 15-fold increase in just over three years, with market capitalisation of these assets reaching around US$2tr in March 2022. Hong Kong sees this rapid growth as evidence that the market is interconnected with the mainstream financial system. The regulator is therefore keen to tighten the existing controls on this area.

To date, however, the regulatory regime for VAs has covered only a subset of activities – largely those with a securities angle. Back in 2017, the territory's Securities and Futures Commission (SFC) imposed regulatory requirements on all entities conducting activities involving VAs where the relevant assets meet the definitions of either securities or futures contracts under the Securities and Futures Ordinance (SFO). Since very few VAs meet either of those definitions, the SFC has only required intermediaries to be licensed and registered if their activities involve actual securities as well as VAs. Entities that trade only non-security VAs do not come under the SFC's regulatory remit.

In November 2018, the SFC issued guidance on the regulatory standards expected on VA portfolio managers and fund distributors and set out a conceptual framework for the potential regulations of VA trading platform operators.

Similarly, in November 2019, the SFC issued a position paper setting out a licensing framework (referred to as the voluntary opt-in regime) for platforms that offer trading of at least one security-type VAs; platforms solely trading non-security VAs are not covered. As of March 2022, the SFC has granted only one VA trading platform licence, to a company that offers a platform with brokerage, exchange, and insured custody for professional investors.

Lately, there have been moves to regulate VAs more comprehensively. In November 2020, and then again in May 2021, the Financial Services and Treasury Bureau (FSTB) announced plans to introduce a new licensing regime to directly regulate all VA exchanges. Under the proposed regulations, any trading platform that facilitates the offer, sale, or purchase of any VA in exchange for money or other VAs will fall within the definition of VA exchanges. Such platforms will need to be licensed by the SFC, as well as to comply with the AML and counter-terrorism financing (CTF) obligations set out in the AML and CTF Ordinance. This means that nearly all VA exchanges operating in Hong Kong will need to be licensed by the SFC; they will be allowed to provide services only to professional investors. The FSTB said that it intended to introduce the legislation to the Legislative Council in 2022.

Initially, the proposed regime will apply only to exchanges dealing in VAs as currently it is the most prevalent VA business, and not to other types of VA service providers (VASPs), such as crypto wallet providers and custodians or peer-to-peer trading platforms. However, flexibility will be built in the licensing regime so that it can be expanded to cover other forms of VA activities if the need arises in the future.

Meanwhile, on 28 January 2022, the SFC and the Hong Kong Monetary Authority (HKMA) issued to banks and SFC-licensed intermediaries a Joint circular on intermediaries' virtual asset-related activities. This circular gives guidance on distributing VA-related products and providing relevant dealing or advisory services. Intermediaries are asked to notify the SFC in advance if they intend to engage in VA-related activities.

On the same day, the HKMA issued a separate circular, Regulatory approaches to Authorized Institutions' interfaces with VAs and VASPs. This proposes not to prohibit authorised institutions (AIs) from incurring financial exposure to VAs if they have adequate risk management controls in place with sufficient oversight by senior management. The type of exposure concerned may include investment, lending against VAs as collateral, or allowing customers to use their credit cards or other payment services to acquire VAs.

Like SFC-licensed intermediaries, AIs intending to launch VA-related products or services should first discuss their plans with the HKMA and any other relevant regulators to obtain feedback on the adequacy of their risk management controls.

Specific considerations for licensed corporations regulated by the SFC

Distribution of VA-related products

VA-related products are highly likely to be considered complex products. In this case, the intermediaries distributing them should normally comply with SFC requirements governing the sale of complex products. This implies, among others, ensuring the suitability of the products, irrespective of whether there has been a solicitation or recommendation, selling restrictions (i.e., they can be offered to professional investors only) and a VA knowledge test. The only exception is for products considered to be complex exchange-traded derivatives which are authorised or approved for offering to retail investors by the respective regulator in a designated jurisdiction. Accordingly, the "professional investors only" restriction is not imposed for the distribution of these products and intermediaries may distribute them without complying with the suitability requirement but still need to comply with the derivative products requirements (i.e., knowledge and sufficient net worth requirements).

VA dealing services

Intermediaries wanting to provide VA dealing services are required to partner only with SFC-licensed VA trading platforms. This requirement applies whether the intermediaries want to introduce clients to the platforms for direct trading purposes or to establish an omnibus account with the platforms. Such services should only be provided to existing clients who are professional investors, and to whom the intermediaries already provided services in relation to Type 1 regulated activity.

Intermediaries should not relay any orders on behalf of their clients to the platforms or hold any client assets, including fiat currencies and client VAs, during the provision of dealing services.

VA advisory services

When providing VA-related advisory services, irrespective of the nature of the VAs, intermediaries are expected to comply with all the regulatory requirements imposed by the SFC. Once again, such services should be provided only to existing clients to whom the intermediaries already provide services in relation to Type 1 or Type 4 regulated activities.

Specific considerations for institutions regulated by the HKMA

Prudential supervision

Institutions must conduct proper due diligence on the VAs to which they will incur exposure. They should understand the legal and financial structure of the providers, the technology behind their creation, and the background of the parties operating the scheme. Other considerations include risk management arrangements and the provenance of any VAs to be acquired for investment.

Based on the information obtained, the institutions should critically evaluate their exposures to different types of risk and put in place appropriate mitigation measures. These measures might include setting prudent limits on their overall exposure to VAs and applying conservative loan-to-value ratios for VAs accepted as collateral. Where residual risks exist, the institutions should set aside sufficient capital to meet prevailing capital requirements applicable to VAs.

AML/CFT and financial crime risk

Effective AML/CFT policies will need to be established, with procedures and controls to manage and mitigate money laundering and terrorist financing risks. Account should be taken of any relevant guidance issued by the HKMA and the Financial Action Task Force.

Investor protection

As noted above, VA-related products are likely to be considered complex products, which means that additional investor protection measures will probably be imposed on the distribution of VA-related products; with investor education strongly encouraged. Firms should observe the guidance issued by the HKMA and the SFC, in particular the joint circular on intermediaries' virtual asset-related activities mentioned above.

United States

If any emerging asset class is looking to break into the traditional financial services realm, then it needs to conquer the US. The country sets the global benchmark for financial services and it would appear that such products are finally emerging as viable options for US customers. The value of the cryptoasset market exceeded US$2.1 trillion in October 2021 with highs of $2.9 trillion – more than Italy's gross domestic product – and its growth doesn't look likely to slow down in 2022.

According to the US Treasury Financial Crimes Enforcement Network, regulatory authorities have not been shy about enforcing regulations related to cryptoassets, with one crypto exchange fined US$110m for failure to detect suspicious transactions and file suspicious activity reports. Meanwhile, the US's federal legislators, state legislators and government agencies continue to outline the framework of a formalised regulatory landscape for the treatment of cryptoassets.

over

US$2.1 trillion

value of the cryptoasset market

October 2021, with **highs of $2.9 trillion**

The basis for this activity is the US Congress's method of determining whether jurisdiction of a cryptoasset lies with the US Securities and Exchange Commission (SEC) or the US Commodity Futures Trading Commission (CFTC). This determination depends on whether the cryptoasset qualifies as an investment contract. In establishing the Howey Test), the Supreme Court formulated the criteria underlying an investment contract:

> *"The test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others. If that test be satisfied, it is immaterial whether the enterprise is speculative or non-speculative or whether there is a sale of property with or without intrinsic value."*

Hence, the four-pronged Howey Test used to determine whether an investment contract exists asks whether there is

a) investment of money
b) in a common enterprise
c) with the expectation of profit, and
d) to be derived from the efforts of others.

If the cryptoasset passes the Howey Test and is deemed an investment contract, it is considered a security and therefore subject to the jurisdiction of the SEC.

Cryptoassets that do not pass the Howey Test would be subject to regulation by the CFTC, which has jurisdiction of the US commodities markets and the majority of swaps and futures. However, as most swaps and futures on cryptoassets would fall within the CFTC's jurisdiction, it's currently unclear as to which specific cryptoassets would meet the definition of a commodity under the US Commodity and Exchange Act. Additionally, the US Treasury Department of Financial Crimes Enforcement Network (FinCEN) and state regulators have jurisdiction under money transmission laws and regulations (more related to cryptocurrency oversight than to cryptoassets).

The US has a fragmented regulatory framework with multiple regulatory agencies whose remit appears to overlap when it comes to cryptoassets. This picture is unlikely to change in the near future.

Specific considerations

AML controls

If your firm is considering engaging in any cryptoasset activities, it's imperative to establish a sound compliance programme with robust AML and know-your-customer (KYC) policies and procedures.

For all assets, financial institutions are required to perform due diligence on customers and monitor and report suspicious activity. However, it's relatively easy for cryptoassets to circumvent normal precautions because they enable anonymous (or at least pseudo-anonymous) transactions that at times do not rely on a third party like a banking institution. This anonymity means cryptoassets are well-suited to illegal activities such as tax evasion, black market transactions, terrorist financing, sanctions avoidance and enabling ransomware payments, and money laundering schemes.

To mitigate the associated risks and avoid breaches of the Bank Secrecy Act, rigorous ongoing transaction monitoring systems should be put in place.

Cybersecurity

Cybersecurity continues to be a major area of interest during US regulators' routine inspections of financial services institutions. As we have seen, cryptocurrencies – and more specifically securitised cryptoassets – enable a level of anonymity, and therefore raise cybersecurity concerns. It's therefore imperative to ensure that your firm has adequate policies and procedures in place, within a sound cybersecurity framework tailored to crypto activity. Firms planning to engage in crypto-related activities need to establish continuous monitoring on a real-time basis to check for cyber attacks.

The Howey Test, outlined above, can help you determine which regulator's jurisdiction applies to your cryptoasset, and hence understand your regulatory obligations. If the crypto product is not deemed a securitised asset, it will be categorised as a currency, regulated under the Department of the Treasury, FinCen and individual state governments. In this case, you will potentially be required to register for a Money Transmitter License (MTL) under each relevant state agency.

Abu Dhabi

Over the past few years, Abu Dhabi has been steadily establishing itself as the Middle East's leading jurisdiction for digital asset service providers.

Fundamental to this success is the Abu Dhabi Global Market (ADGM), a free-trade zone not constrained by the laws that govern other financial activity in the UAE. Governed by the Financial Services Regulatory Authority (FSRA), the ADGM has the goal of becoming a leading innovative hub for the financial services sector.

Managing and promoting digital assets is high on the ADGM's agenda. Bucking the trend of other Middle Eastern territories, in 2018 Abu Dhabi became the first jurisdiction to introduce a bespoke regulatory framework for virtual asset activities, with additional guidance covering digital assets issued in February 2020.

Specific considerations

Before settling on Abu Dhabi as your preferred business destination, it's important to note some areas that the FSRA will focus on when assessing your suitability to operate within the ADGM:

Technology and governance/controls

Distributed ledger technology (DLT) access implications

If you are looking to operate a multilateral trading facility (MTF), some DLTs may have difficulty in transferring digital securities from one party to another if the DLT is permissioned (a closed network where the participants in the network are selected by the operator network).

Market abuse and reporting mechanisms

The ADGM has brought virtual assets under the same scope as traditional securities, meaning trades will need to be assessed for potential breaches e.g wash trading, with the same reporting obligations in place.

Misleading impressions

The regulator expects firms to not create communications or advertisements that provide false or misleading impressions about products. Examples include proposed price movements, expected returns or overall applicability/usability of the token.

Ability to meet annual audit obligations

Third-party audits must verify the amount of digital assets held if applicable to the business activities.

AML and counter-terrorist financing policies and procedures

These are applicable to both FSRA and UAE federal laws.

Possible applicability of the FSRA's Islamic financing rules

The regulator will review whether digital assets offered or distributed by the firm are classified as Shari'a-compliant securities, and therefore subject to additional ruling.

Gibraltar

Gibraltar has maintained a nimble, flexible, and transparent approach to digital assets and to DLT providers seeking European authorisation to offer services. In doing so, it has successfully competed with the many other jurisdictions offering themselves as bases for emerging technologies and innovative financial services. This achievement is even more remarkable when we consider that Gibraltar's regulator presides over a small overseas territory of the UK – and has been a country historically regarded as having taken a somewhat cautious approach to the crypto sector.

Back in January 2018, Gibraltar became one of the first jurisdictions globally to introduce specific legislation targeting DLT providers who used such technology for the "storing or transmitting of value belonging to others". Samantha Barrass, CEO of the Gibraltar Financial Services Commission (GFSC), has stressed the idea that "regulation will bring reputation"; the regulator's hope is that a more unconventional approach will help Gibraltar set itself apart on the world stage.

This strategy already seems to be providing returns for the GFSC. As of 2021, Gibraltar was the territory with the third-highest number of crypto hedge funds, overtaking Luxembourg and Lichtenstein, both of which were ahead of it the previous year.

3rd highest

number of crypto hedge funds

as of 2021, overtaking both Luxembourg and Lichtenstein

Specific considerations

Some issues should be considered before choosing Gibraltar as your preferred location for business. These include:

The GFSC's unique approach to authorising a DLT firm: Applicants go through a detailed three-stage assessment process, and afterwards receive an on-site visit from the regulator to check that processes and controls are as agreed. This thorough process should give customers comfort that those Firms who have received authorisation have passed a stringent review by the Regulator and are therefore able to provide services in a compliant manner.

Passporting rights into the UK: Gibraltar is the only jurisdiction in the world that still benefits from passporting rights into the UK. This means firms with a Gibraltar licence may offer their services to UK clients without applying for an FCA licence. A jurisdiction with a smaller market and limited applications may be able to process applications more quickly than a larger, busier jurisdiction – an important consideration for firms with tight timescales.

GFSC principles and expectations: In a similar way to the Hong Kong regulator, the GFSC has clearly set out its expectations of DLT providers in a set of nine principles (see below) against which any application is likely to be assessed. Importantly, it is also considering adding a tenth principle to provide market integrity standards for digital asset exchanges, in line with defined global standards for providers. A working group of industry leaders has been convened to address this issue.

The nine regulatory principles for DLT providers

1	Business must be conducted with honesty and integrity
2	Firms must pay due regard to the interests and needs of each and all its customers and must communicate with its customers in a way which is fair, clear, and not misleading.
3	Adequate financial and non-financial resources must be maintained
4	Firms must manage and control its business effectively, and conduct its business with due skill, care, and diligence, including having proper regard to risks to its business and customers
5	There must be effective arrangements in place for the protection of client assets and money when it is responsible for them
6	Effective corporate governance arrangements must be in place
7	All systems and security access protocols must be maintained to appropriate high standards
8	Systems must be in place to prevent, detect and disclose financial crime risks such as money laundering and terrorist financing
9	Firms must be resilient and develop contingency plans for the orderly and solvent wind down of business

Switzerland

Against fierce competition, Switzerland has been striving to establish itself as the go-to jurisdiction for digital asset providers in Europe. In recent years, it has seemed to be achieving that aim.

In 2021, the Swiss Stock Exchange obtained regulatory approval for a digital asset exchange. This approval is a world first and a major milestone in the country's journey towards becoming a big player in the sector; it emphasises Switzerland's intention to allow digital asset firms to flourish. There are already said to be more than 950 crypto- and blockchain-related firms operating in the nation, and this figure is expected to grow.

Because digital assets can be classified as securities under Swiss law, firms offering such products are subject to the regulatory framework of the Financial Services Act (FinSA). This means that they need to get licensed as securities firms for their proposed activities.

Specific considerations

Firms looking to commit to operations within Switzerland should consider the following issues:

Secondary trading of products

This could lead to additional licensing requirements under the Financial Market Infrastructure Act (FMIA) if products are classified as securities.

The 'travel rule' for blockchain transactions

This requires specific service providers to ensure that proof of ownership is available for non-custodial wallets over a specified limit.

The Distributed Ledger Technology (DLT) Act 2021

This Act introduced a new licensing category for platforms involved in trading DLT rights. Providing a clear and transparent path to licensing gives additional credibility to securities in which the rights are traded over DLT.

About Bovill

Bovill is a specialist financial services regulatory consultancy, established in 1999 and operating across the world, with offices in the UK, Singapore, Hong Kong, and the United States, with experts spanning all aspects of financial regulation.

Our sole activity is the provision of high-quality, technically focused advice and consultancy services on all aspects of financial services regulation. We aim to develop effective solutions to the complex problems of our clients, and do not offer commoditised advice or services.

Get in touch

Damon Batten
Practice Lead, Capital Markets

dbatten@bovill.com

www.bovill.com

LONDON HONG KONG SINGAPORE NEW YORK