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## Deep Dive: Digital Currency In Malaysia

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Digital Currency (otherwise known as Cryptocurrency) is a blockchain-powered digital asset that is offered and traded on various platforms such as Bitcoin and Ethereum (Digital Currency), which has garnered interest from entrepreneurs and investors all around the globe. Based on a recent study<sup>1</sup>, Malaysia has been rated among the top 20 countries intrigued in cryptocurrency. The study revealed that Malaysia placed 13th with an average of 106,800 online searches about cryptocurrency each year.

However, it is pertinent to note that Digital Currency is not recognised as legal tender nor a payment instrument in Malaysia by Bank Negara Malaysia (BNM) to date, as Digital Currency does not exhibit *universal characteristics of money* due to its volatility and speculative nature affecting its stability as a legal tender.

This alert discusses the regulatory and legislative framework and the future of digital currencies in Malaysia.

### Regulatory Framework

Digital Currency is regulated in Malaysia through the Capital Markets and Services (Prescription of Securities) (Digital Currency and Digital Token) Order 2019 (Prescription Order 2019). Digital assets come in many forms but under the Prescription Order 2019, digital assets are categorised into two particular types which are digital currency and digital token (collectively referred to as Digital Asset). Therefore, all Digital Asset meeting the criteria stipulated in the Prescription Order 2019 will be prescribed as securities for the purposes of securities law in Malaysia.

Pursuant to paragraph 2 of Prescription Order 2019, Digital Currency is defined as a digital representation of value that is recorded on a distributed digital ledger that functions as a medium of exchange and are interchangeable with any

<sup>1</sup> Harizah Kamel, 'Malaysia Among Top 20 Countries Intrigued By Cryptocurrency' (The Malaysian Reserve, 2021) <<https://themalaysianreserve.com/2021/03/16/malaysia-among-top-20-countries-intrigued-by-cryptocurrency/>> accessed 15 March 2022.

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money, including through the crediting or debiting of money to an account. Meanwhile, a digital token is defined as a digital representation that is recorded on a distributed digital ledger, whether encrypted or not. As a result, any Digital Assets that are not recorded on a distributed digital ledger are not covered by the Prescription Order 2019.

## How Are Digital Currencies Deemed As Securities?

Under paragraph 3(1) of the Prescription Order 2019, Digital Currency is deemed to be a security for the purposes of securities laws if:

- (a) It is traded in a place or on a facility where offers to sell, purchase, or exchange the digital currency are regularly made or accepted.
- (a) A person expects a return in any form from the trading, conversion or redemption of the digital currency or the appreciation in the value of the digital currency.
- (b) Is not issued or guaranteed by any government body or central banks as may be specified by the Securities Commission of Malaysia (SC).

## How Are Digital Tokens Deemed As Securities?

Paragraph 3(2) of the Prescription Order 2019 states that a digital token is deemed to be a security for the purposes of securities laws if:

- (a) The person receives the digital token in exchange for consideration.
- (b) The consideration or contribution from the person, and the income or returns, are pooled.
- (c) The income or returns of the arrangement are generated from the acquisition, holding, management or disposal of any property or assets or business activities.
- (d) The person expects a return in any form from the trading, conversion or redemption of the digital token or the appreciation in the value of the digital token.

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- (e) The person does not have day-to-day control over the management of the property, assets or business of the arrangement.
- (f) The digital token is not issued or guaranteed by any government body or central banks as may be specified by the SC.

## Digital Asset Trading

In compliance with the Prescription Order 2019, the SC updated the Recognised Markets Guidelines (RM Guidelines) in 2020 to set out the standards and framework for digital asset platform operators on the Digital Asset Exchange (DAX), i.e. the electronic platform that supports the trading of Digital Assets. DAX operators must register with the SC as a Recognised Market Operator (RMO) before they can lawfully operate as a DAX operator in Malaysia, according to Section 34 of the Capital Markets and Services Act 2007 (CMSA 2007) and the RM Guidelines.

Further, pursuant to Section 7 of the CMSA 2007, members of the public are not permitted to offer, issue or distribute any digital assets in Malaysia without obtaining registration from the SC. Those doing so may be liable and if convicted, be fined up to RM 10 million or face imprisonment for a term not exceeding 10 years or both.

As to date, there are only 4 registered and approved DAX operators, namely Luno Malaysia Sdn Bhd, MX Global Sdn Bhd, SINEGY Technologies (M) Sdn Bhd and Tokenize Technology Sdn Bhd<sup>2</sup>.

## Digital Asset Offering

In Malaysia, digital assets must be issued as securities through a registered Initial Exchange Offering (IEO) platform. IEO is a digital fundraising mechanism in which an issuer provides investors with digital tokens in exchange for monies.

The SC issued the Guidelines on Digital Assets in 2020 in accordance with the CMSA 2007 (DA Guidelines) to regulate the issuance of digital assets for fundraising using IEO platforms. The DA Guidelines outline the eligibility requirements for applicants, as well as the requirements and

<sup>2</sup> Extracted from the List Of Registered Digital Asset Exchanges

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obligations that IEO operators and digital asset issuers must fulfil.

Additionally, pursuant to the DA Guidelines read together with the RM Guidelines:

- (a) Any IEO operator who seeks to facilitate the trading of digital assets on its platform shall first be registered as a DAX operator under the RM Guidelines.
- (b) No DAX Operator shall facilitate the trading of any digital asset unless the SC has approved the trading of the said digital asset.
- (c) Any digital token sought to be traded on any DAX platform shall require SC's prior approval.

## Digital Asset Custody

Under the DA Guidelines, an IEO operator also bears the following obligations in relation to its investors' digital tokens:

- (a) To ensure that the token holders' digital tokens are properly segregated and safeguarded from conversion or inappropriate use by any person.
- (b) To establish and maintain a sufficiently and verifiably secured storage medium designated to store digital assets from investors.
- (c) To establish system and controls for maintaining accurate and up-to-date records of client's digital assets held.

An IEO operator may appoint a Digital Asset Custodian (DAC) registered with the SC to provide custody for the digital tokens, or it may choose to provide its own custody services in order to fulfil these obligations. According to the DA Guidelines, a DAC is a person who provides services such as safekeeping, storing, holding, or preserving custody of digital assets for another person's account, and such services are capital market services for the purposes of Section 76A of the CMSA 2007. An IEO operator who wishes to provide custody for the digital tokens of token holders must be registered with the SC as a DAC, in addition to being registered as an IEO operator.

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## Outlook

It is clear that a collaborative effort by the SC and the BNM in developing a comprehensive regulatory framework for Digital Assets should be implemented to safeguard the stability and legitimacy of Digital Currency. Stakeholders have urged regulators to legalise and regulate the use of recognised digital currencies for the purchase and/or investment in Digital Asset as soon as possible in order to further promote fundraising and investment activities in the Digital Asset field.

Authored by Pupil, Cuthbert Ephraim Chan Pak Hang from the firm's Corporate & Real Estate Transactions practice.

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