

Securities Commission Issues Guidelines on Digital Assets

20 JANUARY 2020

Following on from the issue of Public Consultation Paper No. 1/2019 on the Proposed Regulatory Framework for the Issuance of Digital Assets Through Initial Coin Offerings on 6 March 2019, the Securities Commission Malaysia ('SC') issued the [Guidelines on Digital Assets](#) ('Guidelines') on 15 January 2020.

According to a [media release](#) issued by the SC on the same day, the Guidelines will come into force in the second half of 2020. The SC added that the release of the Guidelines will allow potential issuers, platform operators and investors to familiarise themselves with the requirements in the Guidelines. The SC added that members of the public may also submit feedback to the SC on any matter relating to the Guidelines by 15 May 2020.

The SC has also reminded the public in its media release that no person is permitted to offer or issue any digital tokens in Malaysia until the Guidelines come into force.

This note highlights some of the main requirements set out the Guidelines.

A. OVERVIEW

The Guidelines are divided into three parts. **Part A** sets out the general provisions, **Part B**, the requirements relating to digital token offerings, and **Part C**, the requirements relating to an operator of an electronic platform through which digital tokens are to be offered ('IEO operator').

B. DIGITAL TOKEN OFFERINGS

1. The issuer

An issuer must satisfy the following criteria in order to raise funds through the offering of digital tokens ('issuer'):

a) Incorporation

The issuer must be a company incorporated in Malaysia, but must not be an exempt private company or a public listed company. An unlisted subsidiary or a special purpose vehicle of a public listed company may be an issuer.

b) Place of operations

The issuer must carry out its main business operations in Malaysia.

c) Financial requirements

The issuer must have a minimum paid-up capital of RM500,000. The SC may impose additional financial requirements that commensurate with the nature of the issuer's business.

d) Directors and senior management

- i) An issuer's board of directors must, at all times, have at least two directors whose principal or only place of residence is in Malaysia;
- ii) An issuer must ensure that its directors and senior management are fit and proper, taking into account the criteria in Appendix 1 of the Guidelines and must submit to the IEO operator a fit and proper declaration in respect of such persons.

e) Moratorium on equity

- i) The directors and senior management of an issuer must, in the aggregate, own at least 50% equity holding in the issuer on the date of issuance of the digital tokens;
- ii) Subsequent to the issuance of the digital tokens, the initial directors and senior management may only sell, transfer or assign not more than 50% of their initial equity holding until the completion of the digital token's project;
- iii) Any new director or senior management who purchases equity holding in an issuer after the issue of the digital tokens is not allowed to sell, transfer or assign more than 50% of his equity holding until the completion of the digital token's project.

2. Limit on fundraising

- i) An IEO operator must ensure that the amount raised by an issuer within any continuous 12-month period must not exceed 20 times of the amount of an issuer's shareholders' funds, subject always to a ceiling of RM100 million;
- ii) The issuer must demonstrate to the IEO operator that the gross proceeds to be raised from the digital token offering will be sufficient to undertake the project or business as proposed in the disclosure document to be issued in connection with the digital token offering ('whitepaper');
- iii) The offering is to be on an "all or nothing" basis in that the digital tokens must be fully subscribed. Over-subscription of digital tokens is not permitted. In the case of under-subscription, the IEO operator must return all monies collected from the investors within 14 days from the closing date of the digital token offering.

3. Investment limits

The following limits apply to investments in a digital token offering:

- i) For sophisticated investors: no restriction;
- ii) For angel investors: a maximum of RM500,000 within a 12-month period;
- iii) For retail investors: a maximum of RM2,000 per issuer with a total investment limit not exceeding RM20,000 within a 12-month period.

4. Cooling-off right

- i) An investor who invests in a digital token offering must be given a cooling-off right, except where the investor is a staff of the issuer;
- ii) The cooling-off period must not be less than six business days commencing from the date of receipt of the investor's investment;

- iii) When an investor exercises the cooling-off right, he shall be entitled to a refund equal to the aggregate of the purchase price paid for the digital token and any other charges imposed on the day the digital token was purchased. The refund is to be made by the IEO operator within five business days from its receipt of the notification of exercise of the cooling-off right by the investor.

5. Application for Offerings of Digital Tokens

a) Approval requirement

An issuer must submit its application to an IEO operator for approval in a form and manner specified by the IEO operator. The application must, among other requirements, include a whitepaper containing the information specified in paragraph 5.04 of the Guidelines.

b) Offering of digital tokens

- i) An issuer must only carry out an offering of digital tokens through an IEO operator;
- ii) An issuer must not offer any digital tokens to any person before the approval of the IEO operator has been obtained.

c) Innovative solution or meaningful digital proposition

An issuer must demonstrate in its application to the IEO operator that the digital token's underlying business or project provides an innovative solution or a meaningful digital value proposition for Malaysia. By way of illustration, the Guidelines state that the requirement for innovative solution or meaningful digital value proposition is satisfied if the digital token's project:

- i) provides a solution or addresses an existing market need or problem; or
- ii) improves the efficiency of an existing process or service undertaken by the issuer or the industry,

through the application of distributed ledger technology.

d) Closed loop

If a digital token serves as a payment instrument, it may only be used in exchange for an issuer's goods and services as disclosed in the issuer's whitepaper approved by the IEO operator.

6. The whitepaper

a) Submission of whitepaper

- i) An issuer is not permitted to offer a digital token to any person unless the offer is accompanied by a whitepaper that has been approved by an IEO operator;
- ii) A copy of the whitepaper that has been furnished to the IEO operator must also be furnished to the SC;
- iii) An issuer must ensure that all information submitted or contained in its whitepaper is true and accurate and does not contain any information or statement which is false or misleading or from which there is a material omission.

b) Contents of the whitepaper

- i) A whitepaper must contain such information that would enable an investor to make an informed assessment of the digital token, including the following:
 - A brief description of the directors, senior management, key personnel and advisers, including their names, designations, nationalities, professional qualifications and related experience;
 - The objective or purpose of the digital token offering, including detailed information on the underlying business or project to be managed and operated by the issuer;
 - The key characteristics of the digital token;
 - Detailed description of the sustainability and scalability of the underlying business or project;
 - The business plan of the issuer;
 - The targeted amount to be raised through the digital token offering, and the use and application of the proceeds, illustrated in a scheduled timeline for the utilisation of the proceeds;
 - Any rights, conditions or functions attached to the digital tokens including any specific rights attributed to a token holder;
 - A discussion on the determination of the accounting and the valuation treatments for the digital token including all valuation methodologies and reasonable presumptions adopted in such calculation;
 - Associated challenges and risks and the measures to mitigate the same;
 - Where applicable, the issuer's distribution policy for the digital tokens;
 - A detailed technical description of the protocol, platform and the application of the digital token, as the case may be, and the associated benefits of the technology;
 - Audited financial statements of the issuer, and where they are not available, financial statements or management accounts or information certified by the issuer's senior management;
- ii) A whitepaper must state that Bank Negara Malaysia does not recognise digital tokens as legal tender or a payment instrument regulated by it and that it will not provide any avenue of redress for aggrieved token holders.

7. Obligations of an issuer

a) General

An issuer must, amongst its other obligations:

- i) At all times maintain the prescribed minimum capital requirements;
- ii) Immediately notify the IEO operator and the SC of any failure to comply with any requirement of the Guidelines;

- iii) Retain all relevant documents related to the digital token offering for seven years;
- iv) Provide to the SC any information or assistance as the SC deems necessary relating to the digital tokens.

b) Utilisation of proceeds

- i) An issuer must provide a confirmation to the SC that the drawdowns have been utilised for the purposes stated in the whitepaper;
- ii) An issuer must not make any changes to the drawdown and utilisation of proceeds after the issuance of the digital tokens that affect the token holders' rights unless the prior approval of a majority of the token holders representing 75% of the total amount of tokens held by all token holders present and voting has been obtained.

c) Reporting and audit

- i) An issuer must prepare and cause to be published on the IEO operator's platform an annual report and semi-annual report which contain necessary information that enables token holders to evaluate the performance of the issuer;
- ii) The issuer's report must contain information on the performance of the underlying business or project, including:
 - The amount of digital tokens issued and in circulation;
 - The status of the utilisation of the digital token's proceeds by the issuer;
 - The status of the project;
 - The audited financial statements of the issuer for its latest financial year.

d) Managing conflicts

An issuer must establish a framework which sets out the policies and procedures to effectively and efficiently manage actual or potential issues of conflict and any related party transaction that may arise in the course of the digital token's project.

e) Marketing and promotion

- i) The issuer must ensure that all information disseminated for marketing or promotion is consistent with the contents of the whitepaper;
- ii) The issuer must not engage any third party individual or entity, other than an IEO operator, to endorse or represent the issuer for the intended purpose of marketing, promoting, gaining publicity or soliciting funds for its digital token offering.

f) Material changes

An issuer must inform the IEO operator of any material change that affects the digital token's project or the issuer within 14 days after the occurrence of such event to enable the IEO operator to issue an announcement on the IEO operator's platform.

8. Hosting on multiple platforms

An issuer must not be hosted concurrently on multiple IEO platforms or on an equity crowdfunding platform.

C. THE IEO OPERATOR

1. Registration

- i) A person who wishes to be an IEO operator must be registered with the SC under the Guidelines;
- ii) The SC may register a person as an IEO operator, subject to the person satisfying the requirements in Part C of the Guidelines;
- iii) The application to the SC must be submitted by the applicant itself;
- iv) The application for registration must be in the form specified by the SC in the Guidelines and be accompanied by the relevant documents specified in the Guidelines and any other information required by the SC for the purpose of registration of the applicant as well as the prescribed fees;
- v) An IEO operator registered under the Guidelines is deemed to be registered as a recognised market operator for the purposes of section 34 of the Capital Markets and Services Act 2007.

2. Incorporation

An IEO operator must be a locally incorporated company unless specified otherwise by the SC.

3. Financial requirements

An IEO operator must have a minimum paid-up capital of RM5,000,000. The SC may impose additional financial requirements or other terms and conditions on an IEO operator that commensurate with the nature, operation and risks posed by the IEO operator on the market.

4. Licensing for trading on platform

An IEO operator who wishes to facilitate the trading of digital assets on its platform must also be registered as a digital assets exchange (DAX) operator under the SC's Guidelines on Recognised Markets.

5. Criteria for registration

The SC may register an applicant as an IEO operator if the SC is satisfied that the requirements set out in paragraph 12.01 of the Guidelines have been fulfilled. Among others, these requirements include the following:

- i) The applicant will be able to carry out its obligations under the Guidelines;
- ii) The information or document that is furnished by the applicant to the SC is not false or misleading and does not contain any material omission;
- iii) The applicant and its directors, chief executive, controller and any person who is primarily responsible for its operations or financial management are fit and proper, taking into account the criteria in Appendix 1 of the Guidelines;
- iv) There are no other circumstance which are likely to lead to the improper conduct of business by the applicant or by any of its directors, chief executive, controller or any person who is primarily responsible for the operations or financial management of the applicant;
- v) The applicant will appoint at least one responsible person as required under chapter 13 of the Guidelines;

- vi) The applicant will be able to manage risks associated with its business and operations, including demonstrating the processes and contingency arrangement in the event that it is unable to carry out its operations;
- vii) The applicant has sufficient financial, human and other resources for its operations at all times;
- viii) The applicant has appropriate security arrangements which include maintaining a secured environment pursuant to the SC's Guidelines on Management of Cyber Risk and other relevant guidelines.

6. Directors and Senior Management

- i) An IEO operator which is a public company must have at least one independent director;
- ii) An IEO operator must ensure that its directors, chief executive, controller and any person who is primarily responsible for its operations or financial management are fit and proper, taking into account the criteria in Appendix 1 of the Guidelines and are suitably qualified;
- iii) An IEO operator must notify the SC in writing of any appointment or reappointment of a director, within such time as specified by the SC or prior to any public announcement on such appointment or reappointment, whichever is the earlier;
- iv) An IEO operator must ensure that a director must vacate his position immediately if he becomes subject to any disqualification or becomes otherwise unfit to hold office and must immediately notify the SC of a director's disqualification and when the position is vacated.

7. Responsible Person

- i) An IEO operator must have at least one responsible person who is fit and proper, taking into account the criteria in Appendix 1 of the Guidelines;
- ii) A person appointed as a responsible person must be a chief executive of the IEO operator or a person who is primarily responsible for its operations;
- iii) A responsible person must have a minimum of five years' experience in carrying out due diligence, assessment on business proposals and fundraising or any other relevant experience;
- iv) The responsible person must be the main contact person for the purpose of liaising with the SC and must perform any duty as may be directed by the SC;
- v) Any vacancy in the position of a responsible person is to be filled within three months from the date the vacancy arises.

8. Obligations of the board

The board of directors of an IEO operator must ensure that the IEO operator complies with all the requirements under the Guidelines and any direction issued or any term or condition imposed by the SC.

9. Obligations of the IEO operator

a) Evaluation of digital token offering

In determining whether to approve a digital token offering, an IEO operator must:

- i) Carry out due diligence and critical assessment on an issuer, including:
 - understanding and verifying the business of the issuer to ensure that the issuer does not engage in any business practices that appear to be deceitful, oppressive or improper, whether lawful or not;
 - assessing the fit and properness of the directors and senior management of the issuer;
 - understanding the features of the digital token to be issued by the issuer and the rights attached to it;
- ii) Exercise its own judgment and carry out critical assessment on the issuer's compliance with the requirements of the Guidelines, including whether the issuer will be able to satisfy the requirement to provide an innovative solution or meaningful digital value proposition for Malaysia;
- iii) Assess the issuer's whitepaper; in approving a whitepaper, the IEO operator must ensure that the contents of the whitepaper include the information specified in the Guidelines and are fair, accurate, clear, not misleading and that there is no material omission therefrom;

b) Other obligations of an IEO operator

An IEO operator must also comply with the requirements set out in paragraph 14.03 of the Guidelines. These requirements include:

- i) Making the issuer's whitepaper accessible through its electronic platform;
- ii) Making available through its electronic platform all relevant information relating to an issuer, including the issuer's annual and semi-annual report and any material changes that affect the IEO project or the issuer;
- iii) Taking reasonable steps to monitor the drawdowns by the issuer and that they have been utilised for the purposes stated in the whitepaper;
- iv) Ensuring that its electronic platform is operating in an orderly, fair and transparent manner;
- v) Having in place rules and procedure for the offering of digital tokens on its electronic platform, which rules and any proposed amendments thereto must be approved by the SC before they are enforced;
- vi) Taking all reasonable measures to avoid situations that are likely to involve a conflict of interest with the issuer;
- vii) Disclosing any information and providing any document to the SC as it may require;
- viii) Ensuring that all disclosures are fair, accurate, clear and not misleading;
- ix) Identifying and managing risks associated with its business and operations, including having in place a business continuity plan;
- x) Establishing and maintaining policies and procedures to:
 - Effectively and efficiently manage actual and potential conflicts of interest, including managing of non-public material information; and

- Ensuring compliance with all relevant laws and guidelines, including anti-money laundering and anti-terrorism financing laws and personal data protection laws;
- xi) Immediately notifying the SC of the occurrence of any of the events or circumstances set out in paragraph 14.03(n) of the Guidelines, including among others:
 - Any breach of the terms and conditions imposed by the SC, or any provisions of securities laws, guidelines or the IEO operator's rules, including any alleged or suspected violations of the aforesaid laws or guidelines;
 - Any matter which adversely affects or is likely to adversely affect the IEO operator's ability to meet its obligations or to carry out its functions under the Guidelines;
 - Any material adverse change to the issuer's proposal, including the discovery of any false or misleading statement in relation to the offer, or any material omission of information that may affect token holders, or any material change or development relating to the offering or the issuer.

c) **Risk management**

An IEO operator must comply with the risk management requirements set out in paragraphs 14.05 to 14.09 of the Guidelines, which include identifying and mitigating possible operational risks, having a business continuity plan and carrying out periodic reviews, audit and testing of its systems, policies, procedures and controls relating to risk management and business continuity plan.

d) **Managing conflict of interest**

In relation to managing conflicts of interest:

- i) an IEO operator, including its individual directors and shareholders, must disclose to the public on its platform if:
 - it holds any shares in any of the issuers hosted on its platform; or
 - it pays any referrer or introducer, or receives payment in whatever form, in connection with an issuer hosted on its electronic platform;
- ii) An IEO operator's shareholding in any issuer hosted on its platform must not exceed 30%;
- iii) An IEO operator is prohibited from providing direct or indirect financial assistance to investors and from investing in digital tokens of an issuer that is hosted on its platform.

e) **Safeguarding investors' monies and digital assets**

An IEO operator is required to adopt measures to safeguard investors' monies and digital assets. Among others, these measures include:

- i) Establishing and maintaining one or more trust accounts with a licensed Malaysian financial institution for monies received from investors;
- ii) Ensuring that the trust accounts are administered by an independent trustee registered under the SC's Guidelines on Registration and Conduct of Capital Market Services Providers;

- iii) Releasing the funds to the issuer only after the targeted amount sought has been raised and there is no material adverse change relating to the offer during the offer period;
- iv) Establishing and maintaining a sufficiently and verifiably secure storage medium to store digital assets from the investors;
- v) Having in place arrangements and processes to protect investors' digital tokens from risk of loss, theft or hacking.

f) Register of initial token holders

An IEO operator must maintain a register of initial token holders who subscribed for the digital tokens during the offer period, which register must contain the information prescribed in paragraphs 14.18(a) to 14.18(d) of the Guidelines;

g) Outsourcing of functions

An IEO operator is not prohibited from outsourcing functions to service providers, subject to compliance with the requirements set out in paragraphs 14.19 to 14.24 of the Guidelines, including the requirement that the IEO operator remains accountable for the outsourced functions.

D. COMMENTS

Although the responsibility of evaluating an application for a digital token offering rests with the IEO operator under the Guidelines, the SC has said in the media release that it will work with IEO operators in assessing eligible issuers during the first phase of the implementation of the Guidelines.

The release of the Guidelines has been long awaited and is undoubtedly welcomed by stakeholders in the digital assets space. The Guidelines complement the Capital Markets and Services (Prescription of Securities)(Digital Currency and Digital Token) Order 2019 and the SC's Guidelines on Recognised Markets, the latter of which, among others, set out the requirements for operators of digital asset exchanges. With the recent release of the Guidelines, the regulatory framework for digital assets in Malaysia is now complete.

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