



BERMUDA MONETARY AUTHORITY

CONSULTATION PAPER

DIGITAL ASSET BUSINESS AMENDMENT ACT 2019

31 MAY 2019

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*The views of the digital asset industry and of other interested persons on the proposals set out in this paper and Bill are invited. Comments should be sent to the Authority, addressed to policy@bma.bm not later than **21 June 2019**.*

I. INTRODUCTION

1. The Bermuda Monetary Authority (the Authority) has undertaken to enhance its oversight of Digital Asset Business (DAB) as part of the ongoing development of Bermuda's digital asset regulatory framework. The DAB environment is a new and rapidly evolving space and as such, it is important that Bermuda's regulatory and supervisory framework keeps pace with the rapid rate of change and remains fit for purpose.
2. The Authority is proposing to amend the Digital Asset Business Act 2018 (the Act) to give greater clarity to certain sections and to make other changes that are intended to facilitate more effective administration of the Act.
3. Amendments to the Act will cover, among other things, the following:
 - (a) Amending some definitions and other wording to clarify the Authority's intent in certain sections
 - (b) Extending the Authority's ability to modify applicable fees
 - (c) Inserting a requirement to notify the Authority regarding changes to exemption conditions
 - (d) Effecting changes to the Act and accompanying regulations that are housekeeping matters

II. ENHANCEMENTS TO THE DIGITAL ASSET REGULATORY FRAMEWORK

4. The Authority develops risk-based financial regulations that it applies to the supervision of all of Bermuda's financial sectors including banks, trust companies, investment businesses, insurance companies and DABs. The following proposed changes are intended to improve the overall administration of the Act.

Proposed definition changes

5. The Authority proposes to make the changes to section 2, the interpretation section by removing the definition of "exchange", amending the definition of "qualified custodian" and "digital asset services vendor" and adding new definitions as follows:

"digital asset benchmark" - means any rate, index or figure, made available to the public or published that is periodically or regularly determined by the application of a formula to, or on the basis of, the value of one or more underlying assets or prices, including estimated prices, actual or estimated interest rates or other values, or surveys, and by reference to which the amount payable under a digital asset derivative or the value of a digital asset derivative is determined.

"digital asset benchmark administrator" - means a person that has control over the provision of a digital asset benchmark including administering the arrangements for determining a benchmark, collecting, analysing or processing input data for the

purpose of determining a benchmark and determining a benchmark through the application of a formula or other method of calculation or by an assessment of input data provided for that purpose.

“digital asset derivative” - means an option, a swap, a futures contract, a contract for difference or any other contract or instrument whose market price, value, or delivery or payment obligations are derived from, referenced to or based on a digital asset underlying interest.

“digital asset exchange” - means a centralised or decentralised electronic marketplace used for digital asset distributions and trades, including primary and secondary distributions, with or without payment. It provides or facilitates services such as the following:

- Buying, selling, issuing or trading of digital assets
- Converting digital assets for fiat currency, bank credit or one or more forms of digital assets
- Converting fiat currency or bank credit for one or more forms of digital assets

“digital asset derivative exchange” - means a centralised or decentralised marketplace used for digital asset derivatives issuances, distributions and trades with or without payment.

“digital asset derivative exchange provider” - means a person operating a digital asset derivative exchange and provides the services of—

- (a) creating, selling or otherwise entering into digital asset derivatives contracts
- (b) clearing and settlement of digital asset derivatives

“digital asset services vendor” includes a person that:

- (a) under an agreement as part of its business:
 - (i) can undertake a digital asset transaction on behalf of another person
 - (ii) has power of attorney over another person’s digital asset
- (b) operates as a market maker for digital assets and or digital asset derivatives
- (c) operates as a digital asset benchmark administrator
- (d) provides as a business any service intended to facilitate a transaction involving digital assets

“digital asset trust services” - means a person who carries on the business of acting as a fiduciary, agent, or trustee on behalf of another person for the purpose of administration and management of a digital asset.

“qualified custodian” - means a person recognised by the Authority as having the requisite skills and experience to effect the safe and secure holding of a customer’s digital assets.

Other proposed changes

6. The Authority proposes to expand the scope of DAB in section (2) (2) **“Carrying on digital asset business in Bermuda”** to capture trustees that hold digital assets. While the Authority does not regulate trusts, it does regulate trust companies and because the holding of digital assets requires specialist skills, any trust company that acts as a fiduciary or trustee of digital assets must be recognised by the Authority as a qualified custodian or would need to engage a qualified custodian recognised by the Authority.
7. In order to clarify any confusion regarding the validity period of a licence, in section 10 (2) the Authority is removing after the word “activities”, the words “for the period specified in the licence”. As a result of this removal, only “M” licences will have a defined period attached to them. The Authority is also adding digital asset benchmark administrators, digital asset derivatives exchange providers and digital asset derivative exchanges as defined above to section 10 as businesses subject to the Act and in (10) (c) will replace the term ‘electronic exchange’ with the term ‘digital asset exchange’. The Authority will ensure that its prudential frameworks are developed and prepared to adequately address the expanded scope. Additionally, fees for these new types of exchanges will be same as that for electronic exchanges as listed in the BMA Act.
8. The Authority is proposing to introduce a requirement for companies that seek an exemption order under section 11 of the Act to file an application for such exemption and for such companies to be required to declare annually that they continue to qualify for exemption. This proposal will improve the oversight regime for this sector. This proposal will require the Minister of Finance to amend the existing exemption Order process to provide for persons to notify the Authority of their exempted status and to re-notify annually. Further, section 11 will be also be amended with the exemption in 11(5) (a) deleted. The wording here has been interpreted differently from its intended use and in order to avoid any further confusion, has been removed.
9. In section 15 (2) **“Display and registration of licence”** because of the difference in scope of the two licence classes, the Authority will expand on the information that it will publish on its website to include the type of licence issued, licensed activity/activities, expiry date of the licence and physical address of the business.
10. The Authority is proposing a power that would allow it to modify a fee in cases where companies require other licences in addition to a DAB licence particularly where a business activity crosses between Acts such as investing in digital assets. Presently a company would need both an investment business licence and a DAB licence: requiring two fees. The Authority is of the view that where multiple licences are needed it would be beneficial to the company if the Authority offered a flexible fee structure. The Authority is proposing to amend the Act to add the following:

The Authority may, where it has made a determination-

- (a) exempt a registered person from the requirement to pay any fee under this section, as may be prescribed under the Bermuda Monetary Authority Act 1969
- (b) reduce any fee required to be paid by a registered person under this section by such amount as it considers appropriate, as may be prescribed under the Bermuda Monetary Authority Act 1969
- (c) In granting an exemption from, or reduction of, any fee payment under section (16), the Authority may impose any condition on such exemption or reduction, as it may determine appropriate
- (d) The Authority shall not grant an exemption from, or reduction of, any fee payment under section (16) unless it is satisfied that it is appropriate to do so having regard to the nature, scale and complexity of the business carried on by the registered person

11. The Authority is proposing to clarify its expectation on the handling of clients' digital assets and client monies by licensed DABs. The purpose of this amendment is to make clear that client assets includes both digital assets and client monies. The requirement would be in line with the stated requirements in the "INVESTMENT BUSINESS (CLIENT MONEY) REGULATIONS 2004" and as such would give the Authority a level of consistency across the two Acts. The Authority is intending to set out its expectations in a new Rule that will be issued by year-end 2019.

12. In order to assist the BMA in monitoring compliance with head office principles the Authority is proposing to amend the DAB annual return requirements to include the following information:

- (a) The governance and group structure must disclose (on a legal entity and group basis where applicable) —
 - (i) Structure of the board of directors including names, role, residence and work experience
 - (ii) Structure of the management of the DAB including names, roles, work experience, employee arrangement (for example, confirm whether employees are hired or outsourced, etc.) and description of responsibilities of the chief and senior representative
 - (iii) Terms of reference of the board of directors and its sub-committees
 - (iv) Jurisdiction(s) where the board of directors of the DAB primarily deliberates on activities including, but not limited to—
 - (a) Setting strategic decision of the DAB
 - (b) Determining the DAB's risk appetite
 - (c) Choice of new lines of business, new products, marketplace positioning
 - (d) Assessing solvency needs

- (v) Details of every service provider of the DAB including name, jurisdiction of incorporation, and details of the DAB's operations that are primarily being performed by the service provider
- (vi) Number of employees resident in Bermuda (non-outsourced positions)
- (vii) The name of the jurisdiction(s) where the DAB's board of directors primarily deliberates on matters
- (viii) The jurisdiction(s) where the parent board of directors and chief and senior executives primarily reside
- (ix) The jurisdiction where the DAB's central control functions reside (i.e., finance, compliance, internal audit and risk management)
- (x) Any events which have occurred or decisions made subsequent to the relevant year-end that would, or have, materially changed
- (xi) The jurisdiction of incorporation of any subsidiary or office
- (xii) Information on any amalgamation or acquisition or restructuring, etc. (providing a detailed response and explanation)
- (xiii) A copy of the latest group organisational chart

Housekeeping changes

13. The following changes are a mix of minor technical changes, errors and/or omissions and as such are considered as "housekeeping" changes:
- In section 7 (Prudential and other returns) add the following paragraphs for consistency with other Acts:
 - i. Sections 6, 7 and 8 of the Statutory Instruments Act 1977 shall not apply to Rules made under this section
 - ii. The Schedules to the Rules made by the Authority under this section shall be published separately in the website of the Authority: www.bma.bm
 - In section 10 (b) insert the word "provider" after "payment service" to read as "payment service provider business (PSP)"
 - In section 11 (5) (c) delete the "d" from the word "purpose"
 - In section 31(1) will be corrected to make clear that licensed undertakings are not expected to prepare audited financial statements – rather they are to prepare financial statements to be audited
 - Section 48(2) (b) will be corrected so that where it refers to (1) (a) it will be replaced with (1)
14. In addition to the changes to the Act, the Authority is also proposing some additions to the DAB Code of Conduct to address the prevention of market abuse. In particular, the Authority is proposing to add a new section to the Code designed to prohibit any intentional market abuse. The Authority will also prohibit insider dealing, unlawful disclosure of sensitive information, and market manipulation.

15. Additionally, the Authority is proposing to require that a DAB must have effective systems, procedures and arrangements in place to monitor and detect market abuse and where it suspects that there may exist circumstances to indicate that any violation has occurred, to report any suspicion to the Authority forthwith.
16. The Authority also proposes to extend its power to act in the public interest. More specifically, the Authority proposes to be able to petition the court in circumstances where it deems it appropriate to do so to take any of the following actions:
 - Appoint a person to advise a DAB
 - Appoint a person to take charge of the assets of a DAB, both business and client assets for the purpose of protection of client interest

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3. Amends section 7
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WHEREAS it is expedient to amend the Digital Asset Business Act 2018 to make provision for the enhancement of oversight by the Authority of digital asset service providers by, *inter alia*; introducing new definitions to provide clarity in relation to services to be provided by licensed undertakings; introducing new licensing activities for which persons may seek approval to be licensed by the Authority to carry on in Bermuda; providing a power for the Authority to exempt a licensed undertaking from the payment of any fee imposed under the Bermuda Monetary Authority Act 1969; or to reduce such fees; providing a power for the Authority to publish matters related to licensed undertakings, such as the class of license and duration of the license issued; making consequential amendment to the Bermuda Monetary Authority Act 1969 to introduce application and annual fees for new licensing activities; and for purposes connected with and incidental to those matters;

Be it enacted by The Queen's Most Excellent Majesty, by and with the advice and consent of the Senate and the House of Assembly of Bermuda, and by the authority of the same, as follows:—

Citation

1 This Act which amends the Digital Asset Business Act 2018 (the “principal Act”), may be cited as the Digital Business Amendment Act 2019.

Amends section 2

2 Section 2 of the principal Act shall be amended by—

(a) inserting in the appropriate alphabetical order the following definitions —

“digital asset benchmark administrator” - means a person that has control over the provision of a digital asset benchmark including administering the arrangements for determining a benchmark, collecting, analysing or processing input data for the purpose of determining a benchmark and determining a benchmark through the application of a formula or other method of calculation or by an assessment of input data provided for that purpose.

“digital asset benchmark” - means any rate, index or figure, made available to the public or published that is periodically or regularly determined by the application of a formula to, or on the basis of, the value of one or more underlying assets or prices, including estimated prices, actual or estimated interest rates or other values, or surveys, and by reference to which the amount payable under a digital asset derivative or the value of a digital asset derivative is determined.

“digital asset derivative” - means an option, a swap, a futures contract, a contract for difference or any other contract or instrument whose market price, value or delivery or payment obligations are derived from, referenced to or based on a digital asset underlying interest.

“digital asset derivative exchange” - means a centralised or decentralised marketplace used for digital asset derivatives issuances, distributions and trades with or without payment;

“digital asset derivative exchange provider”; means a person operating a digital asset derivative exchange and provides the services of—

- (a) creating, selling or otherwise entering into digital asset derivatives contracts
- (b) clearing and settlement of digital asset derivatives

“digital asset trust services” - means a person who carries on the business of acting as a fiduciary, agent, or trustee on behalf of another person for the purpose of administration and management of a digital asset.

(b) repealing the definition of “exchange” and substituting the following—

“digital asset exchange” - means a centralised or decentralised electronic marketplace used for digital asset distributions and trades, including primary and secondary distributions, with or without payment. It provides or facilitates services such as the following:

- Buying, selling, issuing or trading of digital assets
- Converting digital assets for fiat currency, bank credit or one or more forms of digital assets
- Converting fiat currency or bank credit for one or more forms of digital assets

(c) repealing the definition of “digital asset services vendor” and substituting the following—

“digital asset services vendor;” includes a person that—

- (a) under an agreement as part of its business—
 - (i) can undertake a digital asset transaction on behalf of another person
 - (ii) has power of attorney over another person’s assets
- (b) operates as market maker for digital assets and or digital asset derivatives;
- (c) operates as a digital asset benchmark administrator;
- (d) provides as a business any service intended to facilitate a transaction involving digital assets

(d) **“qualified custodian”** - means a person recognised by the Authority as having the requisite skills and experience to effect the safe and secure holding of customer’s digital assets.

Amends section 7

3 The principal Act is amended in section 7 by inserting the following new paragraphs after subsection (6) —

“(7) Sections 6, 7, and 8 of the Statutory Instruments Act 1977 shall not apply to Rules made under this section.

(8) The Schedules to Rules made by the Authority under this section shall be published separately on the website of the Authority: www.bma.bm.”.

Amends section 10

4 The principal Act is amended in section 10 (2)—

-
- (a) by deleting the words “for the period specified in the license”;
 - (b) in subparagraph (b) by inserting after “business” the word “provider”;
 - (c) by repealing subparagraph “(c)” and substituting the following—
“(c) operating as a digital asset exchange”;
 - (d) by inserting after subparagraph (d) the following —
“(da) digital asset trust services;
(db) operates as a digital asset derivative exchange provider;”.

Amends section 11

- 5 (1) The principal Act is amended in section 11 by deleting 11 (5) (a);
- (2) in section 11 (5) (c) by deleting “purposed” and substituting the word “purpose”.

Amends section 15

6 The principal Act is amended in section 15 by repealing subsection (2) and substituting the following—

“(2) The Authority shall publish on its website the following information in relation to licensed undertakings—

- (a) a list of all licensed undertakings;
- (b) in connection with a license granted under section 13—
 - (i) the class of license approved;
 - (ii) the digital asset business activity to be carried on under the approved license; and
 - (iii) the expiration date of a license issued;
- (c) the address of the principal place of business.”.

Amends section 16

7 The principal Act is amended in section 16 by inserting the following new paragraph after subsection (4) —

“(5) Subject to subsection (7) and in the case where subsection (4) does not apply, the Authority may, where it has made a determination—

- (a) exempt a licensed undertaking from the requirement to pay any fee under this section, as may be prescribed under the Bermuda Monetary Authority Act 1969;
or

(b) reduce any fee required to be paid by a licensed undertaking under this section by such amount as it considers appropriate as may be prescribed under the Bermuda Monetary Authority Act 1969.

(6) In granting an exemption from, or reduction of, any fee payment under subsection (1), the Authority may impose any condition on such exemption or reduction, as it may determine appropriate.

(7) The Authority shall not grant an exemption from, or reduction of, any fee payment under subsection (5) unless it is satisfied that it is appropriate to do so having regard to the nature, scale and complexity of the business carried on by the licensed undertaking.

Amends section 31

8 The principal Act is amended in section 31 in—

- (a) the title by deleting the word “audited”;
- (b) subsection (1) by deleting the word “audited”.

Amends section 48

9 The principal Act is amended in section 48 (2) (b) by deleting reference to subparagraph “(a)”.

Consequential Amendments

10 Schedule 1 which makes consequential amendments to the Bermuda Monetary Authority Act 1969 has effect.

AMENDMENTS TO THE BERMUDA MONETARY AUTHORITY ACT 1969

The Bermuda Monetary Authority Act 1969 is amended in the Fourth Schedule by inserting—

- (a) under PART B **“Digital Asset Business Act 2018”** after —
- (i) paragraph 2 (e)—
- “(f) The fee payable by a licensed undertaking carrying on digital asset business in accordance with section 10 (2) (da), shall be the lower of amounts calculated under paragraphs (i) and (ii) where—
- (i) equals \$15,000; and
- (ii) the higher of \$15,000 and the 0.00075 multiplied by the estimated client receipts.
- (g) The fee payable by a licensed undertaking carrying on digital asset business maintaining custody of client private keys in accordance with section 10 (2) (db) shall be—
- (i) the lower of amounts calculated under paragraphs (a) and (b) where—
- (a) equals \$450,000; and
- (b) the higher of \$150,000 and the 0.00075 multiplied by the estimated client receipts.
- (ii) where a licensed undertaking does not carry on the digital asset business activity under paragraph (g) (i) above, the annual fee payable shall be the lower of amounts calculated under paragraphs (a) and (b) where—
- (a) equals \$450,000; and
- (b) the higher of \$100,000 and the 0.00075 multiplied by the estimated client receipts.”.
- (ii) paragraph 3 (e)—
- “(f) The annual fee payable by a licensed undertaking carrying on digital asset business in accordance with section 10 (2) (da), shall be the lower of amounts calculated under paragraphs (i) and (ii) where—
- (i) equals \$15,000; and

-
- (ii) the higher of \$15,000 and the 0.00075 multiplied by the estimated client receipts.
 - (g) The annual fee payable by a licensed undertaking carrying on digital asset business maintaining custody of client private keys in accordance with section 10 (2) (db) shall be—
 - (i) the lower of amounts calculated under paragraphs (a) and (b) where—
 - (a) equals \$450,000; and
 - (b) the higher of \$150,000 and the 0.00075 multiplied by the estimated client receipts.
 - (ii) where a licensed undertaking does not carry on the digital asset business activity under paragraph (g) (i) above, the annual fee payable shall be the lower of amounts calculated under paragraphs (a) and (b) where—
 - (a) equals \$450,000; and
 - (b) the higher of \$100,000 and the 0.00075 multiplied by the estimated client receipts.”.
- (b) under PART C **“Digital Asset Business Act 2018”** after —
- (i) paragraph 2 (e)—
 - “(f) The fee payable by a licensed undertaking carrying on digital asset business in accordance with section 10 (2) (da), shall be the lower of amounts calculated under paragraphs (i) and (ii) where—
 - (i) equals \$15,000; and
 - (ii) the higher of \$15,000 and the 0.00075 multiplied by the estimated client receipts.
 - (g) The fee payable by a licensed undertaking carrying on digital asset business maintaining custody of client private keys in accordance with section 10 (2) (db) shall be—
 - (i) the lower of amounts calculated under paragraphs (a) and (b) where—
 - (a) equals \$450,000; and
 - (b) the higher of \$150,000 and the 0.00075 multiplied by the estimated client receipts.

(ii) where a licensed undertaking does not carry on the digital asset business activity under paragraph (g) (i) above, the annual fee payable shall be the lower of amounts calculated under paragraphs (a) and (b) where—

(c) equals \$450,000; and

(d) the higher of \$100,000 and the 0.00075 multiplied by the estimated client receipts.”.

(ii) paragraph 3 (e)—

“(f) The annual fee payable by a licensed undertaking carrying on digital asset business in accordance with section 10 (2) (da), shall be the lower of amounts calculated under paragraphs (i) and (ii) where—

(i) equals \$15,000; and

(ii) the higher of \$15,000 and the 0.00075 multiplied by the estimated client receipts.

(g) The annual fee payable by a licensed undertaking carrying on digital asset business maintaining custody of client private keys in accordance with section 10 (2) (db) shall be—

(i) the lower of amounts calculated under paragraphs (a) and (b) where—

(a) equals \$450,000; and

(b) the higher of \$150,000 and the 0.00075 multiplied by the estimated client receipts.

(ii) where a licensed undertaking does not carry on the digital asset business activity under paragraph (g) (i) above, the annual fee payable shall be the lower of amounts calculated under paragraphs (a) and (b) where—

(a) equals \$450,000; and

(b) the higher of \$100,000 and the 0.00075 multiplied by the estimated client receipts.”.

DIGITAL ASSET BUSINESS AMENDMENT ACT 2019

EXPLANATORY MEMORANDUM

This Bill makes provision for the enhancement of oversight by the Authority of digital asset service providers. It seeks to, *inter alia*; introduce new definitions to provide clarity in relation to services to be provided by licensed undertakings; introduces new licensing activities for which persons may seek approval to be licensed by the Authority to carry on in Bermuda; introduces a power for the Authority to exempt a licensed undertaking from the payment of any fee imposed under the Bermuda Monetary Authority Act 1969 or to reduce such fees; to provide power for the Authority to be more transparent in relation to licensing matters relating to undertakings by publishing matters such as the class of license and duration of the license issued; makes consequential amendment to the Bermuda Monetary Authority Act 1969 to introduce application and annual fees for new licensing activities and for purposes connected with and incidental to those matters:

Clause 1 provides for citation of the Bill.

Clause 2 proposes to introduce new definitions of “digital asset benchmark administrator”; “digital asset benchmark”; “digital asset derivative”; “digital asset derivative exchange”; “digital asset derivative exchange provider”; “digital asset trust services”; repealing and replacing the definition of “exchange” with “digital asset exchange; and to amend the definition of “digital asset services vendor”;

Clause 3 makes provision for section 7 to be amended by disapplying the provisions of section 6, 7 and 8 of the Statutory Instruments Act 1977 to any Rules made under such section and to provide for any Schedules to Rules to be published on the website of the Authority;

Clause 4 provides for clarity to be provided that defined periods shall only apply to class “M” licenses;

Clause 5 proposes to amend section 11 by deleting the word “purpose” and substituting “purposed”;

Clause 6 makes provision for section 15 to be amended by providing a power for the Authority to be transparent re the manner of

licenses issued to undertakings by publishing on its website the additional information of the licensing class, duration of license, the digital asset business activity to be carried on and the address of the principal place of business;

Clause 7 proposes to amend section 16 by inserting a new subparagraph (5) which shall provide powers to the Authority exempt an undertaking from any fee imposed under the Bermuda Monetary Authority Act 1969 or to reduce such fees. The Authority shall not grant such exemption unless it is satisfied with the matters set out under subsection (7);

Clause 8 amends section 31 to provide clarity that licensed undertakings are to prepare financial statement which are to then be audited.

Clause 9 proposes to amend section 48 as a technical house-keeping measure.

Clause 10 makes provision for consequential amendments to the Fourth Schedule to the Bermuda Monetary Authority Act 1969.