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Amendments to Government Orders on Crypto Assets, Digital Securities, etc.

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This newsletter provides an outline of the amendments to the government orders on Crypto Assets, Digital Securities, etc. which came into force on May 1, 2020 (the "Amendments to Government Orders") in relation to the amendments to the Payment Services Act (the "PSA") and the Financial Instruments and Exchange Act (the "FIEA") enacted on May 31, 2019 (the amended legislations are hereinafter referred to as the "Amended PSA" and "Amended FIEA" respectively).

1. Crypto Asset Exchange Services

The Amended PSA changes the term "virtual currency" to "crypto asset," and enhances regulations on crypto asset exchange service providers by developing systems for such providers to ensure the protection of users and clarify the rules.

Details of these regulations are specifically stipulated in the Amendments to Government Orders, specifically the Cabinet Office Ordinance on Crypto Asset Exchange Service Providers (the "Revised Ordinance on Crypto Asset Exchange Services") and FSA Administration Guidelines (the "Revised Guidelines on Crypto Asset").

1-1 Regulation on Crypto Asset Custody Services

1-1-1 Meaning of "Managing Crypto Assets for the Benefit of Another Person"

The Amended PSA designates “managing crypto assets for the benefit of another person” as a type of crypto asset exchange services. Consequently, management of crypto assets without the sale and purchase thereof (“Crypto Asset Custody Services”) is now included in the scope of crypto asset exchange services. Therefore, a person engaging in Crypto Asset Custody Services needs to register itself as a crypto asset exchange service provider[1].

In this context, the Revised Guidelines on Crypto Asset explains the meaning of “managing crypto assets for the benefit of another person” as follows: “although whether or not each service constitutes the management of crypto assets should be determined based on its actual circumstances, a service constitutes the management of crypto assets if an service provider is in a position in which it may transfer its users’ crypto assets (for example if such service provider owns a private key with which it may transfer the users’ crypto assets solely or jointly with its related parties, without the users’ involvement).” Accordingly, it is understood that if a service provider merely provides its users with a crypto asset wallet application (i.e., a non-custodial wallet) and the users manage private keys by themselves, such a service would not constitute a Crypto Asset Custody Service.

1-2 Advance Notification for Amendment of Certain Matters

The Amended PSA requires a crypto asset exchange service provider to notify the FSA before changing any of the following information set forth in its registration: (i) the crypto assets of which trading or custody service are provided; or (ii) the terms and methods of its crypto asset exchange services.

1-3 Special Provisions for Crypto Asset Margin Trading

A crypto asset exchange service provider who executes crypto asset margin trading[2] shall take measures such as disclosure of the terms of its contract on crypto asset exchange in accordance with the relevant Cabinet Office Ordinance as part of its measures to protect users. Any crypto asset exchange service provider that wishes to lend money to its users is required to undergo registration as a moneylending business.

1-3-1 Crypto Asset Margin Trading and Management of Deposited Margin (Leverage Ratio)

When a crypto asset exchange service provider executes crypto asset margin trading with an individual user, it is required to take necessary measures to ensure that the amount of the margin of the user is

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[1] A trust company may be entrusted with crypto assets pursuant to the Trust Business Act without being registered as a crypto asset exchange service provider. On the other hand, a trust bank may not engage in entrustment of crypto assets.

[2] Crypto asset margin trading means crypto asset exchange carried out through granting credit to a crypto asset exchange service user.

not less than the amount calculated by the following formula:

Amount of margin	≧	Amount of crypto asset margin trading (if collectively calculating the amount of margins regarding plural transactions, the total amount regarding such transactions)	×	50%

When a crypto asset exchange service provider executes crypto asset margin trading with a corporate user, it is required to take necessary measures to ensure that the amount of the margin deposited by the user is not less than the amount calculated by the following formula:

Amount of margin	≧	Amount of crypto asset margin trading (if collectively calculating the amount of security deposits regarding plural transactions, the total amount regarding such transactions)	×	Crypto asset risk assumption ratio (if such ratio is not calculated, then 50%)

The calculation method for crypto asset risk assumption ratio is set forth in the public notice by the FSA entitled “Establishing the Calculation Method for Crypto Asset Risk Assumption Ratio in Crypto Asset Margin Trading.” According to the public notice, the crypto asset risk assumption ratio is calculated by a method using the quantitative calculation model, and in that calculation, the one-sided confidence interval is 99% and the holding period is one day or more. When using the quantitative calculation model, historical data satisfying all of the following requirements shall be used:

- Either the figures for the previous 26 weeks or the previous 130 weeks are used, whichever is higher;
- The figures are not calculated by multiplying respective figures by a loanable value; and
- Updated at least weekly.

Further, the Revised Guidelines on Crypto Asset permits outsourcing of calculation of crypto asset risk assumption ratio.

1-3-2 Loss-cutting Transactions in Crypto Asset Margin Trading for Individuals

In order to provide crypto asset margin trading to individual users, crypto asset exchange service providers are obliged to develop a sufficient management system for (i) conducting forced liquidation of open positions, which shall be conducted if the amount of loss accruing to a user at the time of the

liquidation becomes no less than the amount calculated by the method agreed with the user in advance (such settlement, “Loss-cutting Transaction”), and (ii) conducting a Loss-cutting Transaction for such a case.

1-4 Enhancement of Obligation on Crypto Asset Exchange Service Providers to Preserve Users’ Assets

1-4-1 Entrustment of Users’ Money

A crypto asset exchange service provider is required to manage the money of users separately from its own money, and to entrust users’ money to a trust company or any other similar entity (such entrustment, “Segregated User Management Trust”), in accordance with the provisions of the relevant Cabinet Office Ordinance. The agreement concerning the Segregated User Management Trust shall satisfy all of the requirements provided for in the Revised Ordinance on Crypto Asset Exchange Services. Specifically, in an agreement, the entrustor shall be a crypto asset exchange service provider, the entrustee shall be a trust bank, trust company or foreign trust company, and the principal beneficiary shall be a user. In addition, it is a requirement to appoint an expert such as an attorney to serve as the beneficiary’s agent.

1-4-2 Management of Users’ Crypto Assets

A Crypto asset exchange service provider shall manage users’ crypto assets (“Entrusted Crypto Assets”) separately from its own crypto assets. In addition, a crypto asset exchange service provider is required to manage the Entrusted Crypto Assets, in principle, by using a cold wallet that has never been and will never be connected at any time to the internet (a “Totally Offline Wallet”) or with other methods by taking technical safety management measures equivalent to the Totally Offline Wallet[3].

A crypto asset exchange service provider may exceptionally manage crypto assets with other methods, such as hot wallets with multi-signature, if such methods are necessary for ensuring users’ convenience and smooth performance of crypto asset exchange services. However, the JPY equivalent amount of the Entrusted Crypto Assets managed by such other methods must not exceed 5% of the JPY equivalent amount of the total Entrusted Crypto Assets.

1-4-3 Management of Performance Assurance Crypto Assets

In addition, a crypto asset exchange service provider is obliged to hold crypto assets of the same kind and the same quantity as Entrusted Crypto Assets that are managed by other methods than Totally Offline Wallet or its equivalent measure (the “Performance Assurance Crypto Assets”).

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[3] The revised guidelines provides that whether or not “measures equivalent” to the former method above have been taken, in any given case, will be judged for each case based on its circumstances.

Performance Assurance Crypto Assets are the proprietary assets of the crypto asset exchange service provider and must be managed by using Totally Offline Wallet or with other methods by taking technical safety management measures equivalent to the Totally Offline Wallet.

2. ERTRs and Tokenized Securities

2-1-1 Introduction

The FIEA conventionally classified securities into: (i) traditional securities such as shares and bonds (“Paragraph 1 Securities”); and (ii) contractual rights such as trust beneficiary interests and collective investment scheme interests deemed as securities (“Paragraph 2 Securities”). While Paragraph 1 Securities were subject to relatively stricter requirements in terms of disclosures and licensing (registration) as they are highly liquid, Paragraph 2 Securities were subject to relatively looser requirements as they are less liquid.

However, if securities are issued using an electronic data processing system such as blockchain, it is expected that such securities will have higher liquidity than traditional securities such as shares and bonds, regardless of whether they are Paragraph 1 or Paragraph 2 Securities. For this reason, the FIEA was amended last year to introduce a new regulatory framework for securities which are transferable by using electronic data processing systems.

Under the Amended FIEA, securities which are transferable by electronic data processing systems are classified into the following three categories:

(i) Paragraph 1 Securities such as shares and bonds which are transferable by using electronic data processing systems (Tokenized Paragraph 1 Securities);

(ii) Contractual rights such as trust beneficiary interests and collective investment scheme interests, conventionally categorized as Paragraph 2 Securities, which are transferable by using electronic data processing systems (electronically recorded transferable rights (“ERTRs”)); and

(iii) Contractual rights such as trust beneficiary interests and interests in collective investment schemes, conventionally categorized as Paragraph 2 Securities, which are transferable by using electronic data processing systems but have their negotiability restricted to a certain extent (Non-ERTR Tokenized Paragraph 2 Securities).

We explain the definitions, disclosure requirements and licensing (registration) requirements of these new types of securities below.

2-2-1-1 What are “ERTRs”?

ERTRs refer to the rights conventionally treated as “Paragraph 2 Securities” (such as trust beneficiary rights and collective investment scheme interests) that “are represented by proprietary value

transferrable by means of an electronic data processing system (but limited only to proprietary values recorded in electronic devices or otherwise by electronic means)"[4], excluding "those rights specified in the relevant Cabinet Office Ordinance in light of their negotiability and other factors." Here, "those rights specified in the relevant Cabinet Office Ordinance in light of their negotiability and other factors" are presumed to fall under all of the following requirements:

1. Technical measures have been taken to prevent the transfer of the proprietary value to a person other than: (1) qualified institutional investors; or (2) investors eligible for specially permitted business for qualified institutional investors (the so-called "Article 63 Exemption") (For example, (i) listed companies, (ii) corporations with capital or net assets of 50 million yen or more, and (iii) individuals who have investment assets of 100 million yen or more, including crypto assets, and maintain their securities account(s) for over 1 year). 2. Technical measures have been taken to prevent the proprietary value from being transferred without an offer from the owner and an approval from the issuer on each occasion.

As stated below, the key point of the Amended FIEA is that ERTRs will be subject to disclosure requirements and licensing (registration) requirements applicable to Paragraph 1 Securities.

2-2-1-2 Guidelines for the FIEA

As to whether a right constitutes an ERTR, the amendments to the Guidelines for the FIEA provides certain guideline for interpretation.
According to the guidelines, in order for a right to constitute an ERTR, (i) an electronic book-entry (transfer of proprietary value) and transfer of the right must occur (almost) simultaneously. However, even in that case, if (ii) the party to or intermediary of such transaction is unable to know the correct possession status of the seller, the right does not constitute an ERTR.

2-2-1-3 Tokenized Securities

"Tokenized Securities" refer to dematerialized (paperless) securities that are "represented by proprietary value transferrable by means of an electronic data processing system (but limited only to proprietary values recorded in electronic devices or otherwise by electronic means)", which can be specifically classified into the following rights:

[4] For the sake of convenience, "are represented by proprietary value transferrable by means of an electronic data processing system (but limited only to proprietary values recorded in electronic devices or otherwise by electronic means)" is hereinafter paraphrased as "tokenized."

(i) Tokenized Paragraph 1 Securities (such as tokenized shares and bonds);
(ii) ERTRs; and
(iii) Non-ERTR Tokenized Paragraph 2 Securities (See 2-2-1-1 above)

Under the FIEA, both of the rights (i) and (ii) above are treated as Paragraph 1 Securities, whereas the rights (iii) are treated as Paragraph 2 Securities, which creates a significant difference in treatment under disclosure and licensing (registration) requirements.[5]

2-2-2 Disclosure Requirements

2-2-2-1 Public Offering of ERTRs

As a result of the application of disclosure requirements to ERTRs, issuers of ERTRs are in principle required, upon making a public offering or secondary distribution, to file a securities registration statement and issue a prospectus as is the case for Paragraph 1 Securities such as traditional shares and bonds, unless the offering or distribution falls under any category of private placements as stated in “2-2-2-3 Private Placements of ERTRs” below. Any person who causes other persons to acquire ERTRs or who sells ERTRs to other persons through a public offering or secondary distribution must deliver a prospectus to such other persons in advance or at the same time.

2-2-2-2 Annual Securities Reports and Semi-Annual Securities Reports

An issuer who has filed a securities registration statement for a public offering or secondary distribution of certain ERTRs will in principle be required to file annual securities reports and semi-annual securities reports. Matters to be disclosed in annual securities reports are generally the same as the matters to be disclosed in securities registration statements, except that securities offering/distribution information is not required to be stated in annual securities reports.
Even if an issuer has not filed a securities registration statement for a public offering or secondary distribution of securities, where the number of the securities holders subsequently reaches or exceeds a certain number, the issuer may be required to file annual securities reports and semi-annual securities reports thereafter.

[5] Disclosure requirements do not apply to (iii), unless such rights constitute Rights in Securities Investment Business. Even if such rights constitute Rights in Securities Investment Business, disclosure requirements do not apply unless solicitation, as a result of which 500 persons or more come to hold the rights, is conducted. Type II Financial Instruments Business Operators, not Type I Financial Instruments Business Operators, are permitted to engage in the business of handling public offerings and private placements of the rights.

2-2-2-3 Private Placements of ERTRs

Like other types of securities, solicitation of buyers for ERTRs is allowed to be conducted by means of private placements to qualified institutional investors or private placements to less than 50 investors, without assuming the disclosure obligations under the FIEA. Generally, the requirements for private placements of ERTRs are outlined as follows. If the solicitation does not fall under any of the following categories, the issuer will be required to file a securities registration statement or issue a prospectus as stated above.

Private placements to qualified institutional investors[6]	Private placements to less than 50 investors[7]
(i) Solicitation for acquisition is made only to qualified institutional investors.	(i) Solicitation for acquisition has been made to less than 50 persons in the aggregate in the past 6 months.
(ii) The issuer is not required to file an annual securities report. (iii) ERTRs are not “securities for professional investors”.	(ii) The issuer is not required to file an annual securities report. (iii) ERTRs are not “securities for professional investors”.
(iv) Technical measures have been taken to prevent any transfer of ERTRs to a person other than qualified institutional investors.	(iv) Technical measures have been taken to prevent any transfer of ERTRs other than a block transfer or a transfer of fractional ERTRs.

2-2-3 Licensing (Registration) Requirements

2-2-3-1 Type I Financial Instruments Business

As ERTRs constitute Paragraph 1 Securities, any person who engages in the business of the sale, purchase or handling of the public offering of ERTRs is required to be registered as a Type I Financial Instruments Business Operator. For the purpose of new handling of ERTRs or Tokenized Securities, even registered Type I Financial Instruments Business Operators must undergo a registration of change in advance, which means that the making of a subsequent filing is not sufficient.

In light of the higher degree of freedom in designing Tokenized Securities and the higher liquidity of these rights, the Financial Instruments Business Operators who handle Tokenized Securities will be required to develop a control environment appropriate for the characteristics of the relevant Tokenized

[6] Article 2, Paragraph 3, Item 2(a) of the FIEA; Article 1-4, Item 3 of the FIEA Enforcement Order; Article 11, Paragraph 2, Item 1(a) of the Cabinet Office Order on Definitions under Article 2 of the FIEA

[7] Article 2, Paragraph 3, Item 2(c) of the FIEA; Article 1-6 and Article 1-7, Item 2(c) of the FIEA Enforcement Order; Article 13, Paragraph 3, Item 1(a) of the Cabinet Office Order on Definitions under Article 2 of the FIEA

Securities, in addition to the existing control environment, in order to protect investors.
For example, it is required that: (1) appropriate reviews should be regularly conducted, including expert verifications, regarding the risks associated with networks such as blockchain used for Tokenized Securities; (2) since transactions of Tokenized Securities are generally conducted in a non-face-to-face manner, and the rights can be transferred electronically without book-entry transfer institutions, risks should be identified, assessed, and reduced in light of the higher risk of occurrence of terrorist financing and money laundering; (3) system risks should be managed for transactions of Tokenized Securities in light of higher risks of unauthorized access and leakage due to cyberattacks; (4) segregation management should be conducted for transactions of Tokenized Securities in light of the need to deal with the risk of leakage; and (5) in the course of underwriting of ERTRs, internal systems and rules for realizing substantial and accurate examination and reliable verification of examination results should be developed.

2-2-3-2 Self-Offering and Article 63 Exemption

If the issuer of collective investment scheme interests or foreign collective investment scheme interests conducts a public offering or private placement of such interests on its own, the issuer will be required to undergo registration as a Type II Financial Instruments Business Operator, unless such issuer qualifies as a specially permitted business for qualified institutional investors (so-called “Article 63 Exemption”). If those interests are constituted as ERTRs, some of the requirements for the Article 63 Exemption are that the acquirers of the rights to be issued are one or more qualified institutional investors and 49 or less investors eligible for the Article 63 Exemption (See 2-2-1-1 above), and that technical measures have been taken to restrict any transfer of ERTRs.
If ERTRs fall under business-type (non-securities-type) invested business, the issuer may not handle its public offering or private placement or conduct self-offering or private-placement unless the issuer ensures segregation management of invested funds. Particularly, if an investment is made with crypto assets, the contract constituting the relevant ERTRs must stipulate that the management of such crypto assets shall be entrusted to a registered crypto asset exchange service provider.

3. Crypto Asset Derivative Transactions

3-1 Introduction

Proior to the amendment, the FIEA does not regulate derivative transactions related to crypto assets. However, due to the fact that the number of derivative transactions related to crypto assets has increased significantly since around the second half of 2017, the Amended FIEA stipulates that derivative transactions related to crypto assets should be subject to regulation under the FIEA in order to protect users and ensure that only appropriate transactions are conducted. Specifically, crypto assets,

standardized instruments of crypto assets created by a Financial Instruments Exchange, and the prices, interest rates, etc. of crypto assets are now included within the scope of underlying assets of derivative transactions subject to regulations under the Amended FIEA.

3-2 Crypto Asset Derivative Transactions

For the purposes of the FIEA, “Derivative Transactions” is a general term encompassing market derivative transactions, OTC derivative transactions and foreign market derivative transactions. By adding “crypto assets” to the definition of “Financial Instruments,” derivative transactions related to crypto assets (such as futures transactions, CFD transactions, option transactions and swap transactions) will be subject to the provisions of the Amended FIEA. Derivative transactions of exchanging crypto assets for other crypto assets are also covered by the Amended FIEA. In addition, the provisions of the Amended FIEA will apply to derivative transactions that use crypto asset indices as reference indices. Hereinafter, we refer to all these regulated derivatves transactions related to crypto asset as Crypto Asset Derivative Transactions.

The following sections focus on OTC Crypto Asset Derivative Transactions, as most of the Crypto Asset Derivative Transactions in Japan are currently provided over the counter.

3-3 Registration Requirements

Provision of OTC Crypto Asset Derivative transactions related to crypto assets or acting as an intermediary or broker in relation thereto constitutes Type I Financial Instruments Business[8] under the Amended FIEA. Accordingly, a company engaging in these transactions will need to undergo registration as a Type I Financial Instruments Business Operator.

Any entity that intends to become a Financial Instruments Business Operator engaging in Type I Financial Instruments Business is required to meet certain asset requirements, including having:

(i) a stated capital of at least JPY 50 million;
(ii) net assets of at least JPY 50 million; and
(iii) a capital-to-risk ratio of at least 120%.[9]

Crypto Asset Derivative Transactions may include the physical exchange or delivery of crypto assets. If such transactions fall under derivative transactions under the FIEA, such physical exchange or delivery

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[8] Market Derivative Transactions and Foreign Market Derivative Transactions, as well as all intermediary, brokerage, agency services in relation thereto (including intermediary, brokerage, or agency services in relation to the entrustment of such transactions) are deemed to be Type II Financial Instruments Business.

[9] In addition to the asset requirements above, requirements such as personnel requirements, corporate structure requirements, requirements for the establishment of domestic sales offices or business offices, requirements for establishment of internal rules, requirements as to major shareholders, and requirements as to concurrent businesses also need to be satisfied.

of crypto assets will be exempted from the regulations applicable to Crypto Asset Exchange Services under the PSA unless theses transactions entail the management of crypto assets of customers.

Conventionally, the registration requirements under the FIEA are not applicable to non-securities derivative transactions provided to certain professional customers. However, the registration requirements will be applicable to crypto asset derivative transactions, regardless of the type of customers, in light of the high risk nature of the crypto asset derivative transactions.
However, Foreign Crypto Asset Derivative Business Operators [10] conducting OTC Crypto Asset Derivative Transactions with certain professional entities in Japan will be excluded from the registration requirements of the Financial Instruments Business Operators. Such professional entities are:

(i) the government of Japan or the Bank of Japan;
(ii) Financial Instruments Business Operators and financial institutions that engage in Crypto Asset OTC Derivative Transactions in the course of a business;
(iii) financial institutions, trust companies or foreign trust companies (only if they conduct Crypto Asset OTC Derivative Transactions for the purpose of investments or on the account of trustors under trust agreements); and
(iv) Financial Instruments Business Operators who engage in investment management business (only if such entities conduct any act related to investment management business).

3-4 Rules of Conduct

Under the Amended FIEA, Financial Instruments Business Operators that provide their customers with OTC derivative transactions must be subject to various rules of conduct under the FIEA (including the rules prohibiting the provision of false information, the rules prohibiting the provision of conclusive evaluations, etc., the rules prohibiting uninvited solicitation, the rules requiring confirmation as to whether a customer is willing to be solicited, and the rules prohibiting continuing solicitation). In addition to the foregoing, if a Financial Instruments Business Operator engages in Crypto Asset OTC Derivative Transactions, the following acts are prohibited:

(i) entering into a crypto asset related agreement with or soliciting such, or advertising financial instruments transactions related to crypto assets to customers without showing reasonable supporting evidence of certain prescribed facts; and
(ii) soliciting the entering into of a crypto asset related agreement without representing prescribed matters to customers clearly and correctly.

10 Companies that engage in crypto asset derivative transactions in the course of a business in a foreign country under applicable foreign laws and regulations

3-4-1 Loss-cutting Rules

Loss-cutting rules generally refer to a mechanism through which an open position will be compulsorily liquidated by an offsetting transaction to prevent any further losses if the appraised loss reaches a certain level. The amendment to the Cabinet Office Order on Financial Instruments Business, etc. imposes an obligation on Financial Instruments Business Operators to establish and observe loss-cutting rules in connection with OTC Crypto Assset Derivative Transactions with individual customers.

3-4-2 Leverage Regulations

Leverage regulations generally mean regulations obligating business operators to require their customers to deposit margins of an amount that exceeds a certain ratio of the transaction amount (i.e., the notional principal). If a Financial Instrument Business Operator engages in a Crypto Asset Derivative Transactions, it is prohibited from (i) providing transactions without requring their customers to deposit the necessary amount of margins upon entering into a contract with their customers and (ii) continuing transactions without requiring their customers to deposit margins to fill the shortfall in the required deposit, at a certain time on each business day.

The amount of margins to be deposited by a customer will be, if the customer is an individual, 50% of the amount of crypto asset derivative transactions (i.e., the leverage ratio will be up to 2 times) or if the customer is a corporation, the amount of Crypto Asset Derivative Transactions, multiplied by the crypto asset risk assumption ratio as specified in the public notice. This ratio is expected to be based on the calculation by using historical volatilities.

Securities or crypto assets may be used as margins for Crypto Asset Derivative Transactions. The types of crypto assets that may be used as margins and the discount factor applicable to crypto assets used as margins are expected to be specified under the self-regulatory rules of the certified self-regulatory organization.

3-4-3 Segregation of Customers' Assets

The Amended FIEA imposes an obligation on a Financial Instruments Business Operator to entrust its customers' money to a trust company or a trust bank in order to ensure that the money can be refunded to the customers, even in the case of insolvency of the Financial Instruments Business Operator.

3-4-4 Duty to Explain

Since Crypto Asset Derivative Transactions can be highly speculative, certain special provisions concerning the duty to explain, in respect to the crypto asset-related business, have been added to the Amended FIEA.

4. Capital-to-Risk Ratio

4-1 Overview

Financial Instruments Business Operators are required to calculate their capital-to-risk ratio, and report such ratio at the end of each month, as well as when such ratio falls below 140%. If their capital-to-risk ratio falls below 120%, such Financial Instruments Business Operators will be subject to a business improvement order. If their capital-to-risk ratio falls below 100%, such Financial Instruments Business Operators will be subject to an order for suspension of business or rescission of registration.
Capital-to-risk ratio means the ratio of (i) the total amount of capital, reserve and other items prescribed in a Cabinet Officer Order, minus the total amount of fixed assets and other items prescribed in a Cabinet Office Order, versus (ii) the total amounts of items prescribed in a Cabinet Officer Order as amounts corresponding to risks that may arise due to fluctuation of prices of securities held, or risks that may arise due to other factors. As amounts corresponding to risks that may arise due to fluctuation of prices of securities held or risks that may arise due to other factors, the Cabinet Office Order on Financial Instruments Business, etc. specifies the market risk equivalent amount, counterparty risk equivalent amount and basic risk equivalent amount, and specific calculation methods are specified in the relevant public notice. The relevant public notice will be amended, as below, to include risks related to crytpo assets.

4-2 Market Risk

A market risk equivalent amount is an amount calculated by either a standardized approach or an internal control model.
If using a standardized approach, the capital-to-risk ratio of a Financial Instruments Business Operator that holds crypto assets will be calculated under the assumption that the market risk of crypto assets and Crypto Asset Derivative Transactions held by it holds a risk weight of 100%. Meanwhile, if using an internal control model, market risk may be calculated using Value at Risk with the approval of the Commissioner of the FSA.

4-3 Counterparty Risk

Counterparty risk, where a Financial Instruments Business Operator conducts transactions related to crypto assets, is treated in the same manner as other transactions, even though transactions related to crypto assets fall within the category of the highest discount factor to the notional principal.

4-4 Basic Risk

If a Financial Instruments Business Operator holds crypto assets, 100% of the market value of crypto assets that are not managed with cold wallets or other equivalent means must be included in the basic risk equivalent amount.
In addition, if a Financial Instruments Business Operator deposits crypto assets with a third party, the Financial Instruments Business Operator will assume credit risk against such third party in relation to the right to claim the return of such crypto assets. In addition, if such third party does not manage, or it is confirmed that such third party does not manage, such crypto assets with cold wallets or other equivalent means, the Financial Instruments Business Operator is required to calculate the counterparty risk equivalent amount and basic risk equivalent amount related to crypto assets so deposited, respectively.

4-5 Others

If the total amount of the market risk equivalent amount, counterparty risk equivalent amount and basic risk equivalent amount related to a crypto asset or Crypto Asset Derivative Transaction exceeds 100% of the market value of such crypto asset or Crypto Asset Derivative Transaction, such excess amount may be deducted from such total amount.

5. Amendment of Order for Enforcement of the Act on Prevention of Transfer of Criminal Proceeds

In cases of exchange, etc. of crypto assets where the value of the crypto asset pertaining to the exchange, etc. of crypto asset exceeds a certain value, the crypto asset exchange service provider is required to carry out verification at the time of transaction under the Act on Prevention of Transfer of Criminal Proceeds. This value was originally set at 2 million yen, but has since been changed to 100,000 yen.

6. Amendment of Order for Enforcement of the Act on Investment Trusts and Investment Corporations

Under the revision bill to the Order for Enforcement of the Act on Investment Trusts and Investment Corporations, crypto assets (and rights pertaining to crypto-related derivative transactions) do not fall under the definition of Specified Assets. This means that investment trusts and investment corporations may not invest more than 50% of their assets into crypto assets and/or Crypo Asset Derivative Transactions, lest they risk losing their status as investment trusts and investment corporations.

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