

## **Details of Screening for New Registration Application as Virtual Currency Exchange Service Provider**

After the amended Payment Services Act took effect on April 1, 2017, only business operators registered with competent Local Finance Bureau are allowed to operate virtual currency exchange service (i.e. introduced registration system).

(Reference) As of the end of Sep. 2017, 11 applicants have been registered as virtual currency exchange service providers, and 19 are still being examined for registration.

### **For Foreign Operators Applying for Registration:**

When foreign operators apply for registration as virtual currency exchange service providers, they need to consult beforehand with the Local Finance Bureau nearest their main office established in Japan regarding matters such as the details of their business and the documentation they need to prepare. The law requires them to prepare application documents in Japanese or in other languages with a Japanese translation of the documents<sup>1</sup>. For smooth discussion, they are advised, when applying, to involve Japanese-speaking attorneys who are versed in the relevant Japanese laws, such as the Payment Services Act, as well as business practices in Japan.

### **Typical Registration Screening Process:**

In general, each Local Finance Bureau has providers submit preliminary documents of intended application and provide an overview of providers themselves, the virtual currencies they plan to handle and their planned service\*.

After the planned service is found to fall under virtual currency exchange service, each Local Finance Bureau asks the provider to submit a draft registration application and conduct pre-screening to see if, among other things, there are any omissions in the information provided in the application and its internal control systems meet the requirements in Article 63-5 of the Payment Services Act (refusal of registration) and “Guidelines for Administrative Processes” Regarding Virtual Currency Exchange Service Providers (e.g. whether the provider has internal control systems to ensure an appropriate and secure execution of virtual currency exchange service).

\* Including whether

- the virtual currency they plan to handle falls under “virtual currency”
- their service falls under “virtual currency exchange service”

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<sup>1</sup> Note that the required attachments to an application, such as articles of incorporation, internal rules and contracts, created in English are accepted if Japanese translations of their summaries are attached.

as provided in the Payment Services Act

After the consultation prior to application, each Local Finance Bureau asks them to submit a registration application.

**Registration Requirements:**

The law requires applicants to fulfill the following requirements before they are permitted to operate virtual currency exchange service:

- The operator must be a stock company or a foreign virtual currency exchange service provider<sup>2</sup> (limited to foreign companies that have offices in Japan). (As provided in Article 63-5(1)(i) of the Payment Services Act)
- Foreign virtual currency exchange service providers must also be corporations that have a representative in Japan (limited to an individual who has residency in Japan). (Article 63-5(1)(ii) of the Payment Services Act)

Therefore, if a foreign operator that is not a foreign virtual currency exchange service provider intends to operate a virtual currency exchange service in Japan, it must set up a stock company in Japan and that company must be registered as a virtual currency exchange service provider.

When a foreign virtual currency exchange service provider intends to operate a virtual currency exchange service in Japan, it must be a foreign operator that has a local office in Japan AND the representative of the local office must have Japanese residency.

It should be noted that the Companies Act requires that a foreign company register in Japan when it has appointed a representative person in Japan (Article 817(1), 933(1)).

In addition to the above, the following requirements must also be met (Article 63-5(1)(iii)-(x) of the Payment Services Act):

- The provider must have the minimum required financial base (i.e. capitalized at a minimum of 10 million yen, and not in negative net assets) and be equipped with systems for adequate operation and legal compliance, deemed necessary to operate a virtual currency exchange service appropriately and securely.
- The provider must not use a trade name or company name that is identical to one used

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<sup>2</sup> Foreign virtual currency exchange service providers are those operating a virtual currency exchange service under the type of registration deemed the same as that specified in Article 63-2 of the Payment Services Act as provided in a foreign law deemed an equivalent of the Japanese act (Article 2(9) of the Payment Services Act). Foreign virtual currency exchange service providers not registered under Article 63-2 of the act are banned from soliciting acts specified under the items of Article 2(7) of the act, such as trading of virtual currencies and exchange of one virtual currency with another, to Japanese residents (Article 63-22 of the Payment Services Act).

by any other virtual currency exchange service provider.

- The provider must not have had its registration in Japan as a virtual currency exchange service provider revoked or registration as a similar operator revoked based on provisions in a foreign law that is deemed equivalent of the Payment Services Act, in the past five years in either case.
- The provider must never have violated the Payment Services Act, the Law Controlling Contributions, Money Deposits and Interest or equivalent provisions of foreign laws, and never have been fined in Japan or penalized under foreign laws as a result, in the past five years.
- Other businesses operated by the provider must not harm the public interest.
- Directors of the provider must not include disqualified individuals.

**Key Points to be Checked Regarding Organizational System:**

(1) Protective measures for service users (Administrative Guidelines II-2-2-1)

- Whether the provider is equipped with systems to explain, when it explains services or provides information to customers, the information items as provided in the law and ordinance, in accordance with the virtual currencies it handles or the forms of transactions. This includes, for example, whether the provider is equipped with systems to ensure that users are informed about the characteristics of the virtual currency, such as the fact that it is not legal tender or that it carries the risk of loss due to change in its value.

(2) Segregated management of money, virtual currencies deposited by users (Administrative Guidelines II-2-2-2)

- Whether the provider specifies in its internal rules a method of segregated management of money and virtual currencies respectively and such a method is prescribed in the contracts with users.
- Whether the money and virtual currencies belonging to the provider's own assets are clearly separated from those deposited by users in accordance with the method mentioned above and the provider has a system which enables immediate discrimination among deposits belonging to different users. Also, whether the provider is to appropriately verify that such segregation management rule is complied with.

(3) Information technology system risk management (Administrative Guidelines II-2-3-1)

- Whether the provider's board of directors has established a risk management framework, giving sufficient consideration to the possibility that once risk factors materialize, with the development in computer networking, a chain reaction of impact could bring far-reaching and grave results, having serious damage on its operation.
- Whether the provider establishes its IT system risk management framework based on

objective criteria about the development in the IT system risk framework.

Also, whether the provider is regularly reviewing its IT system risk management framework based on the results on monitoring and analysis of IT system problems, outcomes of IT risk management activities and development in technology.

**Time Required for Registration:**

The length of time required for registration can vary, particularly according to the details of the virtual currency exchange service under application and the progress of establishing an operating framework. Generally, however, the process of “Consultation Prior to Application” often takes about three to four months and that of “Application for Registration” typically takes one to two months (similar to the cases of other businesses’ registration).

(Reference) Outline of the Standard Screening Process for Applications for New Registration with the FSA/Local Financial Bureau (published Feb. 10, 2017)

**Cost of Registration Application:**

The applicant must pay 150,000 yen in registration and license tax for each application for registration as a virtual currency exchange service provider. Note that this cost does not include payments to attorneys, office expenses or fees to translate the necessary documents into Japanese.

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