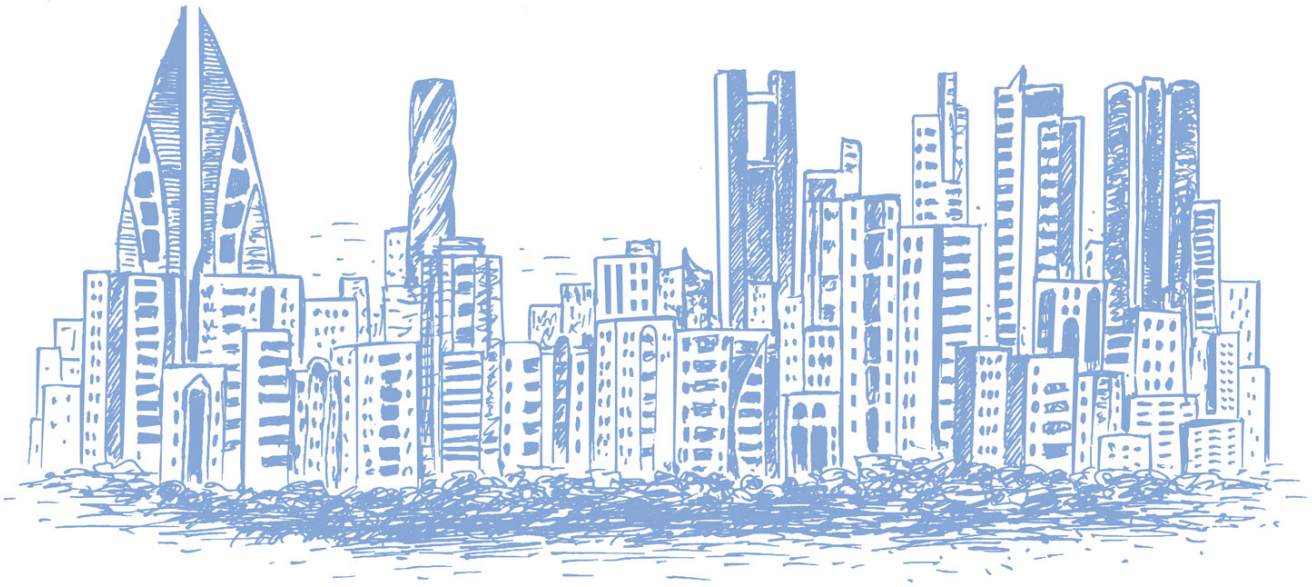


# Central Bank of Bahrain Issues Regulations governing Crypto-Asset Services

Siddharth Goud

s.goud@tamimi.com - Manama, Bahrain



In line with its goal to become the region's leading FinTech hub, the Central Bank of Bahrain ('CBB') has issued comprehensive regulations to govern and license 'Regulated crypto-asset services' in Bahrain. The regulatory framework has been included in Volume 6 of the CBB Rulebook that governs Capital Markets.

The regulations come off the back of the implementation by the CBB of a regulatory sandbox in June 2017. Since the creation of the regulatory sandbox, various crypto-currency related entities have availed of the opportunity and entered the sandbox, thereby working closely with the CBB in testing and refining their technology-based innovative products, services and platforms, in a controlled virtual space without being immediately burdened by the usual regulatory and financial requirements, which would otherwise apply to their activities.

In January this year the CBB invited public consultations and feedback on the draft regulations after which it issued the final regulations ('Regulations') in February. Below we discuss the key features of the Regulations.

## **About the Regulations**

The CBB has issued the Regulations with the aim of minimising the risk of financial crime and illegal use of crypto-assets, as the market for crypto-assets sees an increasing growth and popularity across the globe. The Regulations cover rules for licensing and supervision of 'Regulated crypto-asset services' (defined below); that include trading, dealing, advisory and portfolio management services in 'Accepted crypto-assets' (defined below) either as principal, agent, custodian or as a crypto-asset exchange within or from Bahrain.

## Key Definitions

- **Crypto-assets** have been defined as virtual or digital assets ('tokens') operating on a blockchain platform and protected by cryptography. Tokens have been further classified into:
  - payment/exchange tokens (cryptocurrencies);
  - utility tokens (for specific application);
  - asset tokens (debt or equity claims on the issuer); and
  - hybrid tokens (mixed features of above-mentioned tokens).
- **Accepted crypto-asset** has been defined as a payment token (or crypto-currency) permitted by the CBB for the purposes of undertaking a Regulated crypto-asset service by a Crypto-asset service licensee.
- **Regulated crypto-asset services** means the conduct of any of the following activities:
  - Reception and transmission of order; i.e. receiving orders to buy and/or sell Accepted crypto-assets and transmitting such orders to a third party for execution.
  - Execution of order on behalf of clients; i.e. concluding agreements to buy and/or sell one or more Accepted crypto-assets on behalf of a client.
  - Dealing on own account; i.e. trading against proprietary capital to conclude transactions in one or more Accepted crypto-assets.
  - Portfolio management; i.e. managing a client's portfolio of Accepted crypto-assets with a discretion to invest in one or more Accepted crypto-assets on behalf of the client.
  - Crypto asset custodian; i.e. safeguarding, storing, holding or maintaining custody of Accepted crypto-assets on behalf of a client.
  - Investment advice; i.e. offering tailored and personal recommendation to a client based on the circumstances of the client to buy, sell, exchange or hold Accepted crypto-assets.
  - Crypto-asset exchange; i.e. is a CBB-licensed exchange operating in Bahrain, on which the trading, conversion or exchange of Accepted crypto-assets takes place in accordance with the rules of the crypto-asset exchange.
  - **Crypto-asset service licensee** is a person and/or establishment licensed by the CBB under these Regulations to carry out Regulated crypto-asset services in Bahrain.
  - **Marketing** includes any promotion, offering, announcement, advertising, broadcast or any other means of communication carried out to induce purchase, exchange or acquisition of financial services in return for a payment or other consideration.
  - **Activities** relating to crypto-assets are deemed to be undertaken in or from Bahrain when the person or establishment is incorporated in Bahrain or directly solicits clients within Bahrain.

## Licensing Requirements

Anyone who wishes to market or undertake crypto-asset related activities for business within or from Bahrain will need to obtain a license from the CBB. Applicants must seek to be licensed under the following four categories if they wish to undertake one or more Regulated crypto-asset services:

Category 1	Category 2	Category 3	Category 4
<ul style="list-style-type: none"> <li>• Reception and transmission of orders.</li> <li>• Investment advice.</li> </ul>	<ul style="list-style-type: none"> <li>• Trading in Accepted crypto-assets as an agent.</li> <li>• Portfolio management</li> <li>• Crypto-asset custody service.</li> <li>• Investment advice.</li> </ul>	<ul style="list-style-type: none"> <li>• Trading in Accepted crypto-assets as an agent.</li> <li>• Trading in Accepted crypto-assets as a principal.</li> <li>• Portfolio management.</li> <li>• Crypto-asset custody.</li> <li>• Investment advice.</li> </ul>	<ul style="list-style-type: none"> <li>• Operate a licensed crypto-asset exchange.</li> <li>• Crypto-asset custody service.</li> </ul>

Applications for a license must be filed in the CBB prescribed form and must include the following information (amongst others):

- a business plan specifying the type of business to be conducted;
- application forms for all shareholders and subsidiaries; and
- application forms for all “controlled functions” (further discussed below in this article).

Applicants can combine two or more Regulated crypto-asset services and obtain a license from the CBB for the same, provided the services fall within the same list of services and there is no conflict of interest.

Apart from the non-refundable application fee of BHD 100, licensees will have to bear an annual license fee equivalent to 0.25% of their operating expenses; that can range between BHD 2,000 – BHD 6,000, depending on the operating scale of the applicant. The Regulations set out a 60-day timeframe for the CBB to decide on applications for licenses.

In order to be licensed as a Crypto-asset service licensee, an applicant must be either:

- incorporated as a Bahraini joint stock company; or
- a branch resident in Bahrain of an overseas company duly incorporated under the laws of its home jurisdiction.

The Regulations also allow those persons and/or establishments dealing in Crypto-assets and incorporated in overseas jurisdictions to obtain a license and operate within Bahrain as ‘Overseas crypto-asset service licensees’. An application to set up a branch of an Overseas crypto-asset service licensee will invite the CBB’s scrutiny of its shareholders, management structure, financial position, activities and the Regulations (in its home jurisdiction) that govern its crypto-related activities.

A key aspect of the licensing process is the option for applicants to appoint a representative (such as a law firm or professional consultancy) to prepare and submit applications on their behalf.

## Capital Requirements

All Crypto-asset service licensees in Bahrain must maintain a minimum capital requirement that varies according to the licensing category (specified above):

Licensing Category	Minimum Capital (BHD)
Category 1	25,000
Category 2	100,000
Category 3	200,000
Category 4	300,000

The CBB may, in its discretion, require a licensee to hold additional capital in an amount and form it specifies if it is deemed necessary to ensure the financial integrity of the licensee’s operations.

An Overseas crypto-asset service licensee must also calculate its minimum capital requirements in accordance with those that would apply to it if it were a Bahraini joint stock company.

## Approved persons

Persons assuming ‘controlled functions’ in a CBB regulated Crypto-asset service licensee require the CBB’s written approval. ‘Controlled functions’ include:

- Director;
- Chief executive or General Manager;
- Head of functions;
- Chief Information Security Officer;
- Compliance Officer; and

- Money Laundering Reporting Officer.

For Overseas crypto-asset service licensees, prior approval from the CBB is required for the branch manager (or equivalent) in Bahrain in addition to the same 'controlled functions' described above.

The Overseas crypto-asset service licensee must maintain a local management presence, have its premises in Bahrain and must seek CBB approval if some of its personnel undertaking the 'controlled functions' are not residing in Bahrain.

## **Accepted crypto-assets**

Under the Regulations, the CBB will allow Crypto-asset service licensees (and Overseas crypto-asset service licensees) to undertake services only for Accepted crypto-assets. The CBB will pre-approve crypto-assets by taking into account various factors like:

- technological experience, track record and reputation of the issuer and its development team;
- issuer's anti-money laundering, countering financing of terrorism and cybersecurity systems and controls;
- availability of a reliable multi-signature hardware wallet solution for the asset;
- protocol and the underlying infrastructure of the blockchain technology (i.e. whether it is a separate blockchain with a new architecture system and network or it leverages an existing blockchain for synergies and network effects).

In addition to the above factors, the CBB will also take into consideration factors like the security, traceability/monitoring, resolution mechanisms, geographical distribution, connectivity, market demand/volatility, type of distributed ledger used, the relevant consensus pool of the distributed ledger, innovation and practical applicability/functionality and whether the crypto-asset has been traded on any Dark-net marketplaces.

Applicants applying for a license must submit the details of each crypto-asset that is proposed to be used for their Regulated crypto-asset service. The use of these crypto-assets must be approved as part of the formal application process.

## **Eligible investors**

Crypto-asset service licensees can undertake transactions with/on behalf of persons/establishments only after they have been registered as clients. Eligible investors (or prospective clients) must be a legal entity duly incorporated in Bahrain (or in accordance with laws of the home jurisdictions), or a natural person above the age of 21.

Regulated crypto-asset services can be carried out only if the Crypto-asset license and their clients (i.e. the investors) enter into an agreement which stipulates the following (amongst other aspects):

- the name and address of the Crypto-asset service licensee or the parent company (in the case of an Overseas crypto-asset service licensee);
- the regulatory status of the Crypto-asset service licensee;
- the terms of entering into, terminating and amending the client agreement;
- details of fees, costs and other charges and the basis upon which such costs will be imposed;
- details of the services and products to be provided by the Crypto-asset service licensee;
- details of conflict of interests;
- provisions for complaints handling procedures and/or dispute resolution procedures; and
- the crypto-asset risk disclosure (as mandated by the CBB under these Regulations).

## **Other requirements**

The Regulations also set out provisions relating to professional indemnity coverage, technology standards, cyber security risk requirements, counterparty risk, reporting and notification requirements, etc.

The introduction of these new Regulations is a sign that Bahrain is now open for business to fintech firms across the world dealing in crypto-assets and paves the way for the entry of these businesses and startups into the GCC region, which offers a plethora of untapped opportunities in the realm of blockchain technology.

*Al Tamimi & Company's [Banking & Finance team](#) and [Corporate Commercial team](#) regularly advise on regulations affecting businesses and startups dealing in blockchain technology and crypto-based assets and services. For more information please contact [Rad El Treki \(r.eltreki@tamimi.com\)](mailto:r.eltreki@tamimi.com), [Natalia Kumar \(n.kumar@tamimi.com\)](mailto:n.kumar@tamimi.com) or Siddharth Goud ([s.goud@tamimi.com](mailto:s.goud@tamimi.com)).*