Gary Gensler, US SEC Chair Discusses AI, Fraud, and Investor Protection in Securities Law

On 10 October 2024, Gary Gensler, the Chair of the United States Securities and Exchange Commission (**US SEC**), delivered a statement regarding the risks of fraud and deception in the context of artificial intelligence and its application in finance. His remarks discussed the timeless nature of fraud under US securities law and how new tools, such as AI, present both opportunities and risks. Gensler focused on the evolving challenges AI poses for investor protection, with a specific emphasis on programmable, predictable, and unpredictable harm.

Gensler began by referencing a key historical figure in computer science, Alan Turing, and his famous 1950 question, *"Can machines think?"* He used this reference to highlight the relevance of Turing's question in today's world of securities law, particularly regarding fraud and manipulation. Gensler discussed that although AI represents an advanced tool for today's market participants, fraud remains fraud under US securities law, regardless of the tools used to commit it.

The first category of AI-related harm Gensler discussed was Programmable Harm. He explained that this type of harm occurs when someone uses an algorithm specifically to manipulate or defraud the public. Gensler was clear in stating that if AI models are intentionally programmed to deceive, this constitutes fraud under the US securities law, just as it would if a human actor engaged in such behavior. The risks associated with programmable harm are relatively straightforward, according to Gensler, because they involve deliberate acts of fraud executed through AI.

The conversation became more nuanced as Gensler moved into the second category: Predictable Harm. This category addresses situations where the harm is not explicitly programmed, but where someone deploying an AI model recklessly or knowingly disregards foreseeable risks. Gensler discussed the importance of acting reasonably when using AI in finance. He likened predictable harm to traditional violations such as front-running (trading ahead of customers) and spoofing (placing fake orders), both of which are illegal under US securities law. The core idea here is that even if an AI model is not intentionally designed to defraud, firms deploying such models must ensure that adequate guardrails are in place to prevent predictable risks.

As AI models become more complex, self-learning, and adaptive, Gensler acknowledged that the risks associated with AI may evolve. He pointed out the issue of AI hallucination, where AI models generate inaccurate or misleading results. Despite these technological complexities, Gensler reiterated that firms must still be held accountable for ensuring their AI models operate within the bounds of US securities law and do not expose investors to undue risks.

The third category Gensler discussed was Unpredictable Harm. This category involves risks that may arise from the deployment of AI models where the harm is not foreseeable, due to the nature of the AI system's self-learning capabilities. Gensler recognized the challenges associated with holding firms accountable for harms that may fall outside the realm of predictability. He suggested that while courts may ultimately address these cases, current US securities law already covers much of the programmable and predictable harm that AI models can cause.

Gensler stressed that regardless of how AI evolves, companies deploying these models need to put in place appropriate safeguards. Whether the harm is predictable or not, investor protection remains paramount. He highlighted that companies should not rely on the evolving nature of AI as an excuse for negligence.

Historical Perspective and SEC's Role

Gensler concluded his remarks by invoking Joseph Kennedy, the first Chair of the SEC and the father of President John F. Kennedy. He quoted Joseph Kennedy's famous statement from 90 years ago: *"The Commission will make war without quarter on any who sell securities by fraud or misrepresentation."* Gensler noted that this principle remains relevant today, extending even to those who deploy AI models in finance. The message was clear: fraud, whether carried out by humans or through AI models, will not be tolerated by the US SEC.

(Source: https://www.sec.gov/newsroom/speeches-statements/gensler-transcript-fraud-deception-artificial-intelligence-101024, https://youtu.be/Tym3pO261Gc)

DIFC Courts Launches New Suite of Digital Services, Including Digital Assets Will at GITEX Global 2024

On 15 October 2024, the Dubai International Financial Centre (**DIFC**) Courts announced the launch of a new suite of advanced digital services at GITEX Global 2024, including the Digital Assets Will. This service allows individuals to distribute their digital assets via a non-custodial wallet, built on Hedera Distributed Ledger Technology (**DLT**), providing enhanced security and control. The Digital Assets Will enables individuals to include their digital assets such as Ethereum Classic (**ETH**), Bitcoin (**BTC**), Matic, USD Coin (**USDC**), Tether (**USDT**), Hedera (**HBAR**), and Hedera Token Service (**HTS**) within a non-custodial DIFC Courts wallet. Users retain full control over their assets during their lifetime, allowing them to allocate and transfer digital assets as desired, with the assets distributed as 'specific gifts' upon the Testator's passing. Future updates to the system will likely include support for NFT standards, such as ERC 721, ERC 1155, Ordinals, and HTS.

This new offering complements the existing range of DIFC Courts Wills, which include the Full Will, Property Will, Financial Assets Will, Business Owners Will, and Guardianship Will. Testators registering a Full Will can also choose to incorporate the distribution of their digital assets within the same Will if preferred. The entire Will preparation process, from drafting to registration, is fully digitised and accessible globally. Individuals can create and register their Digital Assets Will through a user-friendly online portal, ensuring seamless service delivery for both residents and international clients.

The Digital Assets Will registration process begins with the Testator selecting either a Single or Mirror Will option. For individuals registering a Single Will, the service costs AED 5,000, while the Mirror Will, intended for married couples registering two Digital Assets Wills simultaneously, costs AED 7,500. The online process involves inputting personal details, specifying Executors and Beneficiaries, and securing an appointment for Will registration. The entire process is conducted through video conferencing, where the Testator and two Witnesses join the call from any location worldwide. The Will is signed electronically on touch-screen devices, securely encrypted, and stored in the DIFC Courts' database. A copy is immediately shared with the Testator.

Upon successful registration, the Testator will receive instructions via email on how to access the DIFC Courts' non-custodial wallet. This wallet allows users to manage and assign their digital assets to Beneficiaries as desired during their lifetime at no extra cost. It is worth noting that any modifications to the Will, such as changing the list of Beneficiaries, will incur a fee.

DIFC Courts have simultaneously launched Digital Notary Service. This service will notarise English documents through multiple service options, including automated self-service, live virtual notary services, or in-person appointments. Users can also choose Primary Source Verification (**PSV**) for authentication purposes. Powered by Hedera Blockchain, the notary service will ensure that notarisation events are timestamped and preserved through DLT, converting documents to NFTs in compliance with ERC20 standards and ensure the integrity and privacy of notarised documents, with encryption methods maintaining confidentiality throughout the process.

The DIFC Courts also introduced the Mediation Service Centre, providing a streamlined digital alternative dispute resolution system. This service allows parties to engage with DIFC-registered mediators, negotiate resolutions, and conduct mediation meetings online through the upgraded AI-enabled Court Management System (**CMS**), or in person.

Justice Omar Al Mheiri, Director of the DIFC Courts, stated that *"In our new digitally driven societies, individuals and businesses are demonstrating increased desire for easily accessible public services. The strong growth momentum arising from the implementation of the Dubai Economic Agenda D33, and the Dubai Digital Strategy, has touched a diverse range of sectors, including government legal services. Our obligation is to deploy the latest emerging technologies to facilitate this growth and demand. Breaking down the boundaries of access to justice sits at the core of our operations and these new digital services provide ease of process across administrative tasks, such as notarisation, to more complex matters involving alternative dispute resolution and inheritance. The DIFC Courts, together with its public and private sector partners, is proud to spearhead some of the UAE's most progressive government legal services, supported by smart technology implementations."*

The development of these digital services is supported by The Hashgraph Association, Deca4 Advisory, and DataFlow Group, which collectively ensured the secure and effective implementation of these innovative legal offerings. Kamal Youssefi, President of The Hashgraph Association, appreciated the importance of this partnership in advancing digital innovation within the UAE's legal infrastructure, while Mohammed Mahfoudh, CEO of Deca4 Advisory, discussed the DIFC Courts' leadership in setting benchmarks for government and semi-government entities globally.

(Source: https://www.difccourts.ae/media-centre/newsroom/difc-courts-launches-new-suite-digital-services-gitex-global-2024-including-digital-assets-will, https://www.difccourts.ae/difc-courts-wills/services/digital-assets-will)

Latvijas Banka Opens Access to Electronic Clearing System for Non-Bank Payment Service Providers

On 16 October 2024, Latvijas Banka announced that it has completed the necessary preparatory work to allow non-bank payment service providers, including licensed payment and electronic money institutions as well as credit unions, to join its Electronic Clearing System (**EKS**). This system is managed by Latvijas Banka and facilitates the execution of instant payments and other financial transactions across the Single Euro Payments Area (**SEPA**) and within the European Union and European Economic Area.

Previously, direct participation in the EKS was restricted to credit institutions and the Treasury. However, from 17 October 2024, this access will be expanded to include non-bank entities, allowing them to participate directly in the execution of payments and to support innovation in Latvia's financial sector, promoting modern, user-friendly, and internationally competitive payment services.

In his statement, Mārtiņš Kazāks, Governor of Latvijas Banka, stated: *"This is an important step towards facilitating the development of payment services in Latvia, giving equal opportunities to all payment service providers in Latvia, and expanding opportunities for the population and companies to use state-of-the-art and innovative payment services. An innovation-supporting infrastructure forms the basis for the development of state-of-the-art and user-friendly financial services. Allowing non-bank payment service providers access to the EKS is one of Latvijas Banka's initiatives for the development of the fintech area. It aims to create an innovative and internationally competitive financial sector in Latvia, one that makes a significant contribution to economic growth."*

For non-bank payment service providers intending to join the EKS, Latvijas Banka outlined some requirements. First, providers must contact Latvijas Banka and conclude a formal agreement for participation. These institutions must also ensure that their systems meet the technical readiness standards, which will be verified through mandatory testing. Further details on the process for joining the EKS are available on Latvijas Banka's official website, where comprehensive guidance on the necessary preparatory steps can be found.

On 14 October 2024, the Council of Latvijas Banka formally adopted amendments to the Regulation on the Participation Procedure in the Electronic Clearing System. These amendments grant non-bank payment service providers the legal right to become direct participants in the EKS, effective 17 October 2024. The legal changes are in line with recent amendments to the Law on Settlement Finality in Payment and Financial Instrument Settlement Systems and the Law on Payment Services and Electronic Money, which now provide for the direct participation of licensed payment and electronic money institutions across Latvia and other EU Member States in national payment systems.

Latvijas Banka has made the necessary technical modifications to the EKS in anticipation of these legislative changes. This includes ensuring secure communication channels and preparing the system for the onboarding of non-bank providers. Institutions seeking to join the EKS will also be required to configure secure information exchange mechanisms and complete a series of compliance checks to align with SEPA payment standards before they go live in the system.

An important area of potential interest is the inclusion of cryptocurrency payment systems in future developments of the EKS. While cryptocurrencies are not explicitly covered by the current framework, there is speculation that the evolving financial landscape could prompt future consultations with Latvijas Banka regarding the integration of digital currencies within the national clearing system. Such developments would, however, require thorough consideration by Latvijas Banka, with careful evaluation of how cryptocurrency payment systems could be accommodated within the existing regulatory structure and whether additional safeguards would be necessary. The inclusive approach promoted by Latvijas Banka is expected to strengthen the country's fintech sector and provide enhanced payment services across the European Union.

(Source: https://www.bank.lv/en/component/content/article/726-news-and-events/17059-latvijas-banka-provides-non-bank-payment-service-providers-with-the-possibility-to-join-the-eks)

Australian Federal Court Rules Harvey Norman and Latitude Misled Consumers in Advertising Campaign

On 18 October 2024, the Australian Federal Court in its judgment ruled that Harvey Norman Holdings Ltd and Latitude Finance Australia engaged in misleading conduct and made false or deceptive representations in relation to a widely promoted 60-month interest-free and no deposit payment method. The ruling stems from a complaint brought forward by the Australian Securities and Investments Commission (**ASIC**), which argued that the advertising campaign failed to disclose the full terms and conditions of the promoted payment method, leading to consumer misunderstanding.

The advertisements in question were run by Harvey Norman and Latitude between January 2020 and August 2021 across various media outlets, including newspapers, radio, and television. These advertisements promoted an interest-free payment method for consumers purchasing goods from Harvey Norman stores, but ASIC alleged that the ads obscured crucial information. The issue at hand was that consumers were not clearly informed they would be required to apply for and use a Latitude GO Mastercard or another eligible Latitude credit card to take advantage of the interest-free payment option.

ASIC raised concerns that the financial implications of obtaining the credit card were not adequately disclosed. Consumers were likely unaware that they would be entering into a continuing credit contract that involved various fees, including establishment fees (until March 2021) and ongoing monthly service fees, which would apply if the statement balance exceeded $10. These details, ASIC argued, were important for consumers to understand the true cost of the "interest-free" offer.

In response to the ruling, ASIC Deputy Chair Sarah Court remarked, *"ASIC took this case because we believed many consumers were unaware of the financial arrangements they were entering into when purchasing products from Harvey Norman. In some cases, this could have led to consumers paying significantly more than expected."* She added that consumers deserve full transparency regarding financial products to assess whether such agreements, including credit cards with high interest rates and fees, align with their financial needs.

Australian Federal Court held that while the advertisements presented the payment method as a straightforward interest-free plan, they failed to disclose the ongoing financial obligations attached to the required credit card. She reiterated that credit card contracts often involve multiple advances of credit, and with fees accumulating monthly, consumers could end up paying far more than they originally anticipated.

Justice Yates, presiding over the case, agreed with ASIC's assertions. The Court found that the advertisements misleadingly presented the payment method as complete and straightforward when, in reality, consumers had to enter into a much more complex financial arrangement. Justice Yates noted, *"Consumers who wished to make such a purchase had to enter into a fundamentally different financial arrangement than the one promoted, namely, a continuing credit contract with Latitude linked to a credit card, whether or not they wanted a credit card."*

This contract required consumers to pay fees beyond the advertised "interest-free" terms, including establishment fees and monthly account service fees, which were not clearly communicated in the advertisements. As a result, the Court ruled that both Harvey Norman and Latitude had breached several provisions of the ASIC Act, including Sections 12DA, 12DB, and 12DF, which relate to misleading or deceptive conduct and false or misleading representations.

Following the ruling, ASIC will seek pecuniary penalties and other relief against both Harvey Norman and Latitude. This case highlights the importance of transparency in financial product advertising and reinforces the need for companies to fully disclose all relevant terms and conditions to consumers.

ASIC's Regulatory Guide RG 234 provides guidelines to help promoters of financial and credit products avoid making false or misleading statements. The ASIC's efforts to protect consumers through the introduction of Design and Distribution Obligations (RG 274) that took effect in October 2021. These obligations require issuers and distributors of financial products to take a consumer-centric approach, ensuring that financial products are designed and distributed in ways that help consumers obtain appropriate products for their needs. ASIC provides educational resources, including through its Moneysmart website, where consumers can learn more about the hidden costs associated with "interest-free" deals and find advice on managing debt.

(Source: https://download.asic.gov.au/media/u2sf1jgw/24-228mr-asic-v-latitude-finance-australia-judgment.pdf, https://asic.gov.au/about-asic/news-centre/find-a-media-release/2024-releases/24-228mr-court-rules-harvey-norman-and-latitude-advertising-misled-consumers/?altTemplate=betanewsroom)

Managing External Shocks: Asia's Experience with Capital Flows – Remarks by Edward Robinson at 2024 Beijing Financial Street Forum

On 18 October 2024, Edward Robinson, Deputy Managing Director (Economic Policy) and Chief Economist at the Monetary Authority of Singapore (**MAS**), delivered a speech at the 2024 Beijing Financial Street Forum, focusing on the theme of "Improving Modern Central Bank Systems, Enhancing Macro-Governance." His remarks addressed the evolving challenges and opportunities that Asia's economies face in managing external shocks, particularly in relation to global capital flows.

Robinson began by reflecting on the shifting dynamics in the global economy, especially following recent negative shocks such as the Covid-19 pandemic, supply chain disruptions, and interest rate hikes in advanced economies. He pointed out that Asia now faces the prospect of easing interest rates, particularly in the U.S. and Europe, which could boost local economies and potentially open up policy space for central banks across Asia to loosen monetary policies if necessary.

He warned that opportunities come with risks, such as the possibility of inflation returning or the threat of a global recession. He discussed the role of capital flows play in transmitting such shocks across economies, especially in Asia, which has historically been vulnerable to volatile inflows and outflows, driven in part by economic conditions in large industrialised economies.

Robinson next elaborated on the concept of the global financial cycle and how it has shaped Asia's financial landscape. He referred to the phenomenon where global economic conditions, especially in advanced economies, often dominate financial conditions in emerging markets. In the past, Asian economies had little policy autonomy when managing the surges and stops of capital flows, which led to procyclical policy responses that exacerbated financial instability.

In his speech, he noted that the recent tightening cycle offers evidence that Asian economies have gained more latitude in managing these global financial cycles while preserving policy autonomy. Robinson pointed to several factors that contributed to this shift, including synchronised global monetary tightening and the preemptive actions taken by Asian economies to contain inflation. These actions helped stabilise capital flows and avoid the extreme volatility seen in previous episodes.

The MAS economist highlighted the importance of stronger buffers in ASEAN economies during the recent period of monetary tightening. Many ASEAN nations benefited from positive foreign direct investment trends, robust current accounts, and the recovery in key sectors, which helped reduce reliance on foreign capital. Additionally, ASEAN economies made significant strides in deepening their local currency asset markets, allowing for greater domestic participation and reducing vulnerability to external shocks.

Robinson also discussed the role of macroprudential measures in mitigating financial stability risks. Over the years, ASEAN policymakers have expanded their toolkits to curb excess leverage, limit balance sheet mismatches, and manage asset bubbles. When faced with currency depreciation pressures earlier in the year, these economies used discretionary policies, including targeted foreign exchange interventions, to manage currency volatility and capital outflows.

Looking at longer-term trends, Robinson presented findings from recent research by the MAS, showing that the influence of external global financial cycles on capital flows to Asia has significantly diminished over the past 15 years. From 1995 to 2010, nearly half of the variation in capital flows to Asia could be attributed to external factors, but that figure has since dropped to around 10%. This improvement suggests that Asian policymakers now have more room to maneuver in responding to domestic shocks.

Despite these encouraging developments, Robinson cautioned that the global synchronisation of economic variables remains intact. While capital flows may have become less linked to external cycles, other economic factors, such as GDP growth and domestic interest rates, have become more dependent on global financial conditions. This suggests that other transmission channels, such as trades in currency and interest rate derivatives, may now play a larger role in transmitting external shocks to emerging markets.

In addressing policy considerations, Robinson stressed that capital flows do not always respond in a way that brings balance to economies. Instead, short-term yield-seeking behavior and external push factors often drive capital movements. In this context, he argued that inflation targeting, supported by strong fiscal policies, remains a key strategy for managing external shocks, complemented by foreign reserves and liquidity buffers to protect the financial system from sudden outflows.

Concluding his remarks, Robinson highlighted Singapore's unique approach to managing price and financial stability. The MAS operates with a dual mandate for both monetary and macroprudential policy, with monetary policy focused on price stability and macroprudential policy targeting financial stability. Singapore's exchange rate-based monetary policy allows for flexibility in managing volatile capital flows, while macroprudential policies prevent excessive credit buildup, particularly in the property sector.

Robinson closed by discussing the importance of international cooperation in securing financial stability. He strongly stated that domestic policies alone cannot shield economies from external shocks, and cooperative measures, such as international swap lines and liquidity support from major economies, play a vital role in mitigating the effects of global financial volatility and stressed that a coordinated approach to macroeconomic, macroprudential, and structural policies is essential for fostering long-term, sustainable growth in Asia.

(Source: https://www.mas.gov.sg/news/speeches/2024/managing-external-shocks)

Joint Statement on Enhanced Timeframe for New Listing Applications Announced by HK SFC and HKEX

On 18 October 2024, the Hong Kong Securities and Futures Commission (**HK SFC**) and The Stock Exchange of Hong Kong Limited (**HKEX**), a subsidiary of Hong Kong Exchanges and Clearing Limited (**HKEX**), announced the introduction of an Enhanced Timeframe for the New Listing application process aimed to strengthen and improve the clarity, transparency, and efficiency of the application process for prospective issuers.

Over recent years, the HK SFC and the Exchange have made progress in enhancing the New Listing application process by offering greater transparency. Since 2023, additional vetting statistics have been published, and all relevant guidance has been consolidated into a Guide for New Listing Applicants to streamline the application process and ensure quality listings on the Hong Kong Exchange, while upholding public interest.

The Enhanced Application Timeframe now provides a more defined schedule for regulatory review of New Listing applications submitted by applicants and their sponsors. The HK SFC, in its role as the statutory regulator, oversees the process under the Hong Kong's Securities and Futures Ordinance (**SFO**) and the Hong Kong's Securities and Futures (Stock Market Listing) Rules (**SMLR**). It works in close coordination with the Exchange, which is responsible for decisions regarding the suitability for listing and compliance with the Hong Kong's Listing Rules.

Under this enhanced process, New Listing applications that meet all regulatory requirements will be processed in a maximum of two rounds of regulatory comments by both the HK SFC and the Exchange. The time taken by each regulator to review the application and raise any material concerns will not exceed 40 business days. Following the resolution of any concerns, the application will proceed to the Listing Committee Hearing. Applicants and their sponsors are expected to address all comments and finalise the listing documents within 60 business days, with the entire process being completed within the six-month application validity period.

For eligible A-share listed companies that meet specific criteria, such as a minimum market capitalisation of HK$10 billion and compliance with A-share listing regulations for at least two years, an Accelerated Timeframe is available. This process limits the review to one round of regulatory comments and reduces the assessment period to 30 business days. However, if material regulatory concerns are raised, the application will revert to the standard procedures.

In cases where Applications Require a Longer Process, such as when there are material regulatory concerns or incomplete responses to regulatory feedback, the HK SFC and the Exchange will engage directly with applicants and sponsors. If deficiencies persist after two rounds of comments (or one round for A-share listed companies), the regulators may issue formal requisition letters, further extending the application process until all issues are resolved.

The Enhanced Application Timeframe is expected to improve the efficiency of the listing process and provide greater certainty for issuers and their advisers. Michael Duignan, the SFC's Executive Director of Corporate Finance, expressed strong support for the initiative. Similarly, Katherine Ng, HKEX's Head of Listing, stated that the streamlined application process would provide much-needed clarity and efficiency for potential applicants. The HK SFC and the Exchange have also committed to continuing to seek market feedback to further enhance the listing process. The Enhanced Application Timeframe applies to all New Listing applications submitted after the date of this joint statement.

(Source: https://apps.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=24PR172)

UK FCA Publishes Blog on Cryptoasset Registrations: Building Strong Foundations for the Future

On 18 October 2024, Val Smith, Head of Payments and Digital Assets at the UK's Financial Conduct Authority (**UK FCA**), published a blog discussing the UK FCA's approach to registering crypto firms and the importance of maintaining high standards under the Money Laundering Regulations. Smith addressed concerns that the UK FCA's rigorous registration process could be stifling innovation, while also reinforcing the need to protect consumers and ensure the integrity of financial markets.

In her blog, Val Smith began by acknowledging criticisms that the UK FCA's standards for crypto firms may be perceived as overly strict. However, she stated that the UK FCA's commitment to tackling financial crime is paramount. Allowing firms with lax controls could pave the way for money laundering, terrorism financing, and other illicit activities. She made it clear that the UK FCA never rejects applications without due consideration, but remains firm in its dedication to protecting the financial system from being misused.

She explained that the UK FCA's role is to prevent the "race to the bottom," where lowering standards could lead to dangerous and unstable growth in the crypto sector. Instead, the UK FCA's focus is on creating a crypto industry built on solid, trusted foundations. By holding firms to high standards, the UK FCA is fostering an environment where innovation can thrive sustainably and securely, with long-term growth prospects.

Smith also highlighted the importance of trust in the financial system, stating that universal standards are essential to building a competitive and thriving crypto sector in the UK. She acknowledged the unique challenges that crypto firms face when navigating new regulatory processes but assured that the UK FCA actively supports firms by offering guidance, pre-application meetings, and practical examples to help them through the registration process.

According to Smith, no two registration applications are the same. The UK FCA's assessment of each firm goes beyond just the systems they have in place. The UK FCA also considers the operational environment, the people behind the firm, and the customers they intend to serve. This individualised approach means that the time required to process each application varies depending on the complexity and specifics of the firm.

Smith concluded by reiterating that the number of crypto firms being registered will continue to be a focus for public and industry scrutiny, but the UK FCA's priority remains clear: protecting consumers and the financial system. The UK FCA is committed to supporting firms that meet the required standards, while filtering out those that pose a risk. By upholding regulations such as the MLRs, the UK FCA is not only addressing current challenges but also ensuring a robust and competitive crypto sector for the future.

(Source: https://www.fca.org.uk/news/blogs/cryptoasset-registrations-building-strong-foundations)

UK FCA Imposes Restriction on Business Agent Limited after Second Supervisory Notice

On 22 October 2024, the United Kingdom's Financial Conduct Authority (UK FCA "the Authority") imposed restrictions on Business Agent Limited, preventing the firm from conducting any regulated activities. These actions are based on the concerns over the firm's handling of client funds and non-compliance with regulatory standards, particularly in relation to its Nextcrowd platform. The restrictions are imposed after the Second Supervisory Notice issued on 10 September 2024 deals with serious failings in the firm's management of client money, violations of UK ISA regulations, and due diligence, prompting the UK FCA to intervene to protect consumers and maintain financial market integrity.

This notice was the result of ongoing regulatory concerns and followed an earlier First Supervisory Notice issued on 22 July 2024. The UK FCA's review of Business Agent Limited revealed several significant failings in its operations, prompting the imposition of strict requirements to protect consumers. These included restrictions on the firm's ability to conduct regulated activities without prior written approval from the Authority, along with obligations to notify relevant stakeholders about these restrictions.

The Second Supervisory Notice was issued after the UK FCA reviewed the firm's representations, submitted following the First Supervisory Notice, but concluded that the concerns remained unresolved. The firm's operations posed a continuing risk to consumers, particularly regarding its management of client funds and compliance with United Kingdom's ISA regulations. As a result, the UK FCA determined that the initial restrictions should remain in place and that additional steps were needed to prevent further harm.

The UK FCA's review revealed troubling practices at Business Agent Limited. One of the issues was the firm's unauthorised handling of client money. Despite a regulatory requirement that it must not hold or control client funds, the firm had been receiving and managing these funds without the necessary permissions. This was a clear breach of the United Kingdom's Client Money Asset Sourcebook (**CASS**) rules, which are designed to ensure that clients' funds are properly safeguarded and not exposed to undue risk. The UK FCA also identified issues

related to the firm's compliance with United Kingdom's Individual Savings Account (**ISA**) regulations. Business Agent Limited had been receiving United Kingdom's ISA subscriptions into accounts that were not correctly set up under the relevant regulations which according to UK FCA jeopardised the security of client investments.

In addition to these financial management issues, the UK FCA found that the firm lacked effective systems and controls to manage key operational risks. Business Agent Limited had failed to put in place adequate measures to identify and manage potential conflicts of interest. These conflicts, if unmanaged, could have compromised the firm's decision-making processes and harmed its clients' interests. The firm had not conducted adequate due diligence on the investments listed on its Nextcrowd platform, raising concerns about the quality and reliability of the investment opportunities it was offering to clients.

The UK FCA also noted the firm's failure to provide requested information about individuals associated with the business. This lack of transparency was a breach of the regulatory obligation to deal with the Authority in an open and cooperative manner. There were potential breaches related to the approval of financial promotions, with the firm possibly failing to comply with rules regarding the promotion of non-mass-market investments. These failures to disclose important information and to meet regulatory requirements raised serious concerns about the firm's overall governance and regulatory compliance.

As a result of these ongoing concerns, the UK FCA imposed restrictions on Business Agent Limited. The firm is prohibited from conducting any regulated activities without the UK Authority's prior written consent, effectively halting its operations. Additionally, the firm was required to notify its financial service providers and clients about the restrictions, ensuring transparency about the firm's limitations. The UK FCA also required the firm to safeguard all client money properly and provide weekly updates to the Authority in the form of bank statements, allowing the UK FCA to closely monitor the firm's financial activities.

The notice also put restriction on Business Agent Limited's role as an ISA Manager. With this restrictions in place, the firm could no longer act in this capacity, and investors who had ISAs managed by the firm were advised to contact Business Agent Limited directly to address any concerns. Although the restrictions applied primarily to the firm's platform operations, investors were encouraged to reach out to the issuers of their investments to determine if their assets were impacted by the firm's regulatory failings.

The breaches identified by the FCA against Business Agent Limited were serious and include violations of provisions such as the United Kingdom's Client Money Asset Sourcebook (**CASS**), UK ISA Regulations, and multiple principles of the UK FCA's Principles for Businesses (**PRIN**). UK FCA flagged the firm's failure to manage conflicts of interest, protect client assets, and maintain transparency with the regulator were significant breaches. The firm's non-compliance with United Kingdom's SUP 16.31.5R(1)(b), which requires timely notification of financial promotions was also duly covered in the supervisory notices.

The UK FCA's action against Business Agent Limited was due to the firm's failure to meet the Threshold Conditions outlined in the United Kingdom's Financial Services and Markets Act 2000. The firm was deemed to be failing, or likely to fail, to meet both the Suitability and Business Model Threshold Conditions. These regulatory standards ensures that a firm operates in a manner that protects consumers and the broader financial market. The firm's failure to manage client funds properly, its non-compliance with ISA rules, and its inability to conduct due diligence or manage conflicts of interest indicated a business model that posed a risk to its clients.

(Source: https://www.fca.org.uk/news/news-stories/fca-imposes-restrictions-business-agent-limited, https://www.fca.org.uk/publication/supervisory-notices/second-supervisory-notice-business-agent-limited-2024.pdf)

US CFTC to Hold a Commission Open Meeting on 29 October 2024

On 22 October 2024, the U.S. Commodity Futures Trading Commission (**US CFTC**) announced that it will conduct an open meeting on 29 October 2024, from 10:00 a.m. to 4:30 p.m. EDT at its Washington, D.C. headquarters, located at Three Lafayette Centre, 1155 21st Street N.W. This meeting will provide an opportunity for the public to attend in person or virtually through a live stream on the US CFTC website or its YouTube channel. During the session, US CFTC will discuss important regulatory matters, including final rules related to operational resilience for futures commission merchants, swap dealers, and major swap participants. The agenda also includes the investment of customer funds by futures commission merchants and derivatives clearing organisations, the development of recovery and orderly wind-down plans for derivatives clearing organisations, and updates on the

Commission's Fall 2024 Unified Agenda. The meeting will cover compensation structures for US CFTC executives and supervisors. The US CFTC has provided virtual access instructions and ensured that materials presented during the meeting will be available to the public online.

Announced by US CFTC Chairman Rostin Behnam, the meeting will be open to the public, offering various options for participation. Members of the public can attend the meeting in person, listen by phone, or view the proceedings via a live stream on the US CFTC's official website, and the meeting will be streamed on the US CFTC's YouTube channel for broader accessibility. The meeting will cover regulatory topics of importance to the futures and swaps markets.

The US CFTC will consider a number of issues during the meeting, including the Final Rule on Operational Resilience Framework for Futures Commission Merchants, Swap Dealers, and Major Swap Participants. This rule ensures that these entities have systems in place to withstand and recover from operational disruptions. The US Final Rule on the Investment of Customer Funds by US Futures Commission Merchants and Derivatives Clearing Organisations will be reviewed, aiming to safeguard customer assets by setting clear standards for how funds can be invested.

Another item on the agenda is the US Final Rule on Derivatives Clearing Organisations (**DCOs**) Recovery and Orderly Wind-down Plans. This rule will outline the necessary plans for DCOs to manage severe financial distress, ensuring that functions continue and that resolution planning is effective. The US CFTC will also review its Fall 2024 Unified Agenda Submission, which will detail its regulatory priorities and planned actions for the upcoming year. Furthermore, the Commission will discuss US CFTC Executive and Supervisor Compensation Structures, focusing on how the agency compensates its senior leaders and supervisors, an essential topic for maintaining talent and leadership within the organisation.

The agenda for the meeting, along with detailed instructions for virtual participation, will be made available on the Commission's website ahead of the meeting. Call-in participants who wish to listen by phone will need to provide their first and last name, along with their affiliation if applicable. Materials presented during the meeting, if any, will also be accessible online, ensuring transparency and public access to key regulatory information.

In the event of any changes to the time, date, or venue for the meeting, the US CFTC will post updated information on its website. Those requiring special accommodations to attend the virtual meeting due to disabilities are encouraged to contact the US CFTC by emailing press@cftc.gov to make the necessary arrangements.

This open meeting represents an important opportunity for the public and stakeholders to engage with the US CFTC on critical regulatory decisions that impact futures commission merchants, swap dealers, derivatives clearing organisations, and the broader market. The decisions made during this session will contribute to shaping the future regulatory landscape for the financial markets under the US CFTC's jurisdiction.

For additional information, members of the public can contact Christopher Kirkpatrick, the Secretary of US CFTC at 202-418-5964.

(Source: https://www.cftc.gov/PressRoom/PressReleases/8999-24, https://www.cftc.gov/media/11511/Federal-Register102224/download)

UK FCA Launches Crackdown on Illegal Finfluencers for alleged Targeting of Young Investors

On 22 October 2024, the United Kingdom's Financial Conduct Authority (**UK FCA**) escalated its efforts to combat financial misconduct on social media, targeting 20 so-called "finfluencers" as part of a new initiative to curb illegal financial promotions. These social media influencers, popular among young followers, are being interviewed under caution by the UK FCA. The authority also issued 38 alerts against various social media accounts suspected of promoting financial products unlawfully. Finfluencers, a term used to describe influencers who promote financial services and products to their online followers, have come under the scrutiny of UK FCA after they gained popularity in recent years. Many finfluencers present themselves as successful investors, flaunting luxurious lifestyles and encouraging their audiences to follow their investment strategies. With nearly two-thirds (62%) of 18- to 29-year-olds following influencers and 74% of those expressing trust in their advice, the potential for harm is substantial. The UK FCA's concern is that many of these finfluencers are not authorised to provide financial advice, yet they influence a vulnerable demographic prone to making impulsive financial decisions.

The rise of finfluencers has led to an increase in scams and investment failures among young people. These influencers often promote high-risk investment products, such as Contracts for Difference (**CFDs**). CFDs are speculative financial instruments that allow investors to bet on the price movements of various assets, including foreign currencies. While these products can offer significant returns, they are also highly leveraged, meaning that investors can lose more than their original investment. The UK FCA has long warned of the risks associated with CFDs, noting that 80% of retail investors lose money when trading them.

The UK FCA's action comes at a time when the number of young victims of financial scams is rising, and the role of finfluencers in promoting these schemes is becoming increasingly problematic. Many finfluencers fail to adequately explain the risks involved in the products they promote, which can result in followers making uninformed and dangerous financial decisions. Steve Smart, joint executive director of enforcement and market oversight at the UK FCA, discussed the responsibility these influencers carry, stating, 'Finfluencers are trusted by the people who follow them, often young and potentially vulnerable people attracted to the lifestyle they flaunt.' He added 'Finfluencers need to check the products they promote to ensure they are not breaking the law and putting their followers' livelihoods and life savings at risk.'

The UK FCA's recent crackdown follows an investigation into illegal financial promotions on social media. Earlier in 2024, the UK FCA brought charges against nine individuals involved in promoting an unauthorised foreign exchange trading scheme through Instagram. The scheme, allegedly operated between 2018 and 2021, involved unregulated financial promotions of CFD products, targeting young investors. Among those charged was Emmanuel Nwanze, accused of running an unauthorised investment scheme and promoting it through the Instagram account @holly_fxtrends. According to the UK FCA, Nwanze and Holly Thompson, another defendant, provided advice on buying and selling CFDs without the necessary UK FCA authorisation.

In addition to Nwanze and Thompson, several other influencers with large number of social media followings were allegedly paid to promote the unauthorised scheme. These include Biggs Chris, Jamie Clayton, Lauren Goodger, and others, who collectively have millions of followers. All of these individuals face charges related to issuing unauthorised financial promotions, a violation of Section 21 of the United Kingdom's Financial Services and Markets Act 2000. Breaching this section is a criminal offence punishable by fines and imprisonment of up to two years.

Court proceedings against these individuals began in mid-2024, with initial hearings taking place at Westminster Magistrates' Court. On 13 June 2024, six of the defendants appeared in court, where some, including Nwanze and Thompson, pleaded not guilty. Others, such as Lauren Goodger and Eva Zapico, did not enter pleas at the time. Subsequent hearings were scheduled, with a plea and trial preparation hearing set for 11 July 2024 at Southwark Crown Court.

The UK FCA has warned and tried to raise awareness that these finfluencers violated provisions of the United Kingdom's Financial Services and Markets Act 2000, which prohibits unauthorised individuals from promoting financial products or schemes. The legal case against them discusses the risks posed by unregulated financial advice on social media. In particular, the UK FCA alleges that these finfluencers exploited their influence over their young, impressionable followers to promote high-risk products without adequately explaining the potential downsides.

For consumers, especially young people, the UK FCA offers guidance on how to avoid falling victim to such schemes. The authority urges individuals to check its warning list of unauthorised firms and individuals before making any financial decisions. It also encourages the public to visit its InvestSmart page, which provides helpful information for making safer investment choices. The UK FCA has also published detailed guidance on the proper conduct of financial promotions on social media, hoping to curb the misuse of these platforms for promoting risky and unlawful investments. By targeting illegal promotions and issuing clear guidance on financial communications, the UK FCA aims to ensure that consumers, especially young people, are not misled into making risky investments based on unreliable advice from unauthorised individuals.

(Source: https://www.fca.org.uk/news/press-releases/fca-cracks-down-illegal-finfluencers, https://www.fca.org.uk/news/press-releases/finfluencers-charged-promoting-unauthorised-trading-scheme)

Denmark's Tax Law Council Proposes Consistent Taxation Framework for Crypto Assets

On 23 October 2024, the Danish Tax Law Council published a comprehensive report recommending changes to the taxation of crypto assets in Denmark. The report, titled "*Finansielle Kryptoaktiver*", focuses on standardising the taxation framework to align with the growing prevalence of crypto investments among Danish citizens. With an estimated 300,000 Danes owning some form of crypto asset, the report addresses the need for more consistent and transparent tax regulations that reflect the unique nature of these digital assets. The recommendations outlined in the report are expected to lead to a legislative proposal in early 2025.

The report discusses the importance of addressing the current tax system's limitations, particularly concerning the inconsistent application of tax laws to crypto assets. Presently, crypto investments fall under various tax regimes, depending on how they are classified. This fragmented approach has caused confusion among investors, many of whom struggle to calculate their tax liabilities accurately. The existing tax system also fails to account for the decentralized nature of crypto trading, which often occurs outside traditional financial institutions and regulated platforms. The Danish Council's recommendation is to simplify this complex framework by unifying the tax treatment of all crypto assets, thus ensuring that investors are subject to the same rules regardless of the type of asset they hold.

Crypto assets, as described in the report, include a wide range of digital representations of value or rights that are stored and traded electronically using distributed ledger technology (**DLT**), such as blockchain. The report explains that crypto assets can take many forms, including cryptocurrencies like Bitcoin, which are decentralized and not backed by a central authority, and stablecoins, which aim to maintain a stable value by being pegged to a fiat currency or other assets. Utility tokens, which provide access to services within specific blockchain ecosystems, are also considered part of this growing market. These assets are typically traded on both centralized and decentralized platforms, adding further complexity to their tax treatment.

In an effort to provide clarity, the report outlines several definitions related to crypto assets and the technology that underpins them. Distributed ledger technology is described as a decentralized database used to verify and record transactions, while blockchain is a specific type of DLT where transactions are grouped into blocks and linked together in a chain. This technology ensures transparency and security, making it the foundation for most crypto assets. The report also discusses mechanisms such as Proof of Work (**PoW**) and Proof of Stake (**PoS**), which are used to validate transactions on the blockchain and reward participants with newly generated crypto assets.

Certain exemptions and special cases are also covered in the report. For example, the treatment of crypto assets received as gifts, or through blockchain forks, requires specific attention. A fork occurs when a blockchain splits into two, often resulting in holders receiving new tokens. The report recommends that such tokens should not be taxed at the point of receipt but only when they are sold or otherwise realized. Similarly, airdrops, free distributions of crypto assets, should be treated as taxable when the assets are sold, not when they are first acquired.

One of the issues addressed in the report is the taxation of gains and losses from crypto transactions. Under the current system, gains from crypto assets may be taxed under different regimes, depending on whether the assets are classified as speculative investments or financial contracts. This has led to situations where investors face tax liabilities on gains even if they have incurred losses overall. The Council proposes moving to a mark-to-market taxation model, where the value of crypto assets is assessed at the end of each tax year. Investors would be taxed on any appreciation in value, even if they have not sold the assets. Conversely, losses would be deductible, creating a more balanced tax framework.

The move to a mark-to-market model is expected to simplify tax reporting for frequent traders, as it removes the need to track every individual transaction. Instead, taxes would be based on the annual market value of the assets held. However, this model also introduces potential challenges, such as liquidity concerns. Investors may find themselves owing taxes on unrealized gains—gains that exist on paper but have not been converted into cash through the sale of the asset. The Council acknowledges this issue and recommends implementing measures to mitigate it, such as allowing losses to be carried forward to offset future gains.

In addition to addressing domestic tax concerns, the report places emphasis on international tax regulations. The Council highlights the need for Denmark to align its crypto tax laws with broader global efforts, particularly within the European Union. Two key international frameworks are discussed: the Markets in Crypto-assets Regulation (**MiCA**) and the DAC8 directive. MiCA aims to harmonize the legal treatment of crypto assets across EU member states to ensure that crypto exchanges and service providers follow consistent rules regarding investor

protection and transaction reporting. DAC8 directive focuses on enhancing transparency by mandating the exchange of tax-related information between EU countries. This directive will make it easier for tax authorities to track cross-border crypto transactions and ensure accurate reporting.

The Council's recommendations aim to create a more transparent and equitable tax system for crypto investors by adoption of the mark-to-market taxation model for all crypto assets, aligning them with the treatment of other financial contracts. The Council also suggests that exchanges and platforms that facilitate crypto transactions be required to report their customers' activities to tax authorities. This would improve the ability of authorities to monitor crypto transactions and ensure that investors are complying with their tax obligations.

The report concludes with outlining the legislative changes that are expected to be introduced in early 2025. These changes will likely include mandatory reporting requirements for crypto exchanges, as well as the formal adoption of DAC8 and MiCA frameworks into Danish law. The Council proposes that the new tax rules should take effect no earlier than 1 January 2026, allowing time for investors and the financial industry to adapt to the changes. Once implemented, these rules will ensure that crypto trading is subject to a standardized and transparent tax regime, benefiting both investors and tax authorities.

(Source: https://skat.dk/en-us/individuals/shares-and-securities/tax-on-cryptocurrency-know-the-rules-and-avoid-a-tax-bill, https://skm.dk/ministeriet/om-skatteministeriet/publikationer-fra-skattelovraadet/rapport-om-finansielle-kryptoaktiver, https://skm.dk/media/5lwjf5qv/finansielle-kryptoaktiver.pdf)

This newsletter is for information purposes only

This newsletter and the information contained herein is not intended to be a source of advice or credit analysis with respect to the material presented, and the information and/or documents contained in this newsletter do not constitute investment advice.

Cryptocurrency markets are highly volatile and speculative in nature. The value of cryptocurrencies can fluctuate greatly within a short period of time. Investing in cryptocurrencies carries significant risks of loss. You should only invest what you are prepared to lose.

The content on this newsletter is for informational purposes only. You should not construe any such information or other material as legal, tax, investment, financial, or other advice. Nothing contained on our newsletter constitutes a solicitation, recommendation, endorsement, or offer to buy or sell any cryptocurrencies, securities, or other financial instruments.

We do not guarantee or warrant the accuracy, completeness, or usefulness of any information on this site. Any reliance you place on such information is strictly at your own risk. We disclaim all liability and responsibility arising from any reliance placed on such materials by you or any other visitor to this newsletter, or by anyone who may be informed of any of its contents.

Your use of this newsletter and your reliance on any information on the site is solely at your own risk. Under no circumstances shall we have any liability to you for any loss or damage of any kind incurred as a result of the use of the newsletter or reliance on any information provided on the newsletter. Your use of the newsletter and your reliance on any information on the site is governed by this disclaimer and our terms of use.

If you do not wish to receive this newsletter please let us know by emailing us at
unsubscribe@charltonslaw.com

CHARLTONS QUANTUM

Hong Kong Office

Dominion Centre 12th Floor
43-59 Queen's Road East
Hong Kong

enquiries@charltonslaw.com
www.charltonsquantum.com
www.charltonslaw.com
Tel: + (852) 2905 7888
Fax: + (852) 2854 9596