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법무법인(유) 세종

Virtual Asset User Protection Act and Its First Market Manipulation Case

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A. Implementation and Key Details of the Virtual Asset User Protection Act

The Virtual Asset User Protection Act (the "Act"), enacted after nearly two years of deliberation, was passed by the National Assembly last year and took effect on July 19, 2024. The Act aims to regulate unfair trading practices in the virtual asset industry and enhance user protection. It outlines the following three key provisions:

1. Protection of User Deposits and Virtual Assets

Virtual asset service providers ("VASPs") are required to, among others:

- Segregate user deposits from their own assets and deposit or entrust them with a reputable institution;
- Maintain and store user records;
- Obtain insurance against hacking and system disruptions;
- Establish reserve funds; and
- Retain transaction records for 15 years.

2. Regulation of Unfair Trade Practices

VASPs must:

- Continuously monitor suspicious transactions; and
- Report any suspected unfair trade practices to financial authorities (being the Financial Services Commission and the Financial Supervisory Service);

Such unfair trade practices include price manipulation, fraudulent or deceptive transactions, and the use of undisclosed material information. Those found guilty of unfair trade practices may become subject to imprisonment of at least one year or fines ranging from three to five times the amount of illicit gains.

3. Supervisory and Enforcement Authority of Financial Authorities

The Act authorizes the financial authorities to supervise, inspect, and enforce VASPs' compliance of the Act. In case of non-compliance, the financial authorities may, among others, issue corrective orders (including for suspension of operations), impose fines or refer the relevant cases to law enforcement authorities.

B. The First Unfair Trade Practice Case under the Act – Market Manipulation

The financial authorities have finalized subordinate regulations, including the presidential decree of the Act, the Virtual Asset Industry Investigation Regulations, and detailed enforcement rules. They are actively investigating unfair trade practices in the virtual asset industry, with dedicated teams of 9 and 17 members at the Financial Services Commission and the Financial Supervisory Service, respectively.

On November 1, 2024, the financial authorities announced the completion of an investigation into a suspected market manipulation case that began on October 25, 2024. This case was subsequently referred to the prosecution via an expedited procedure, marking the first unfair trade case to be prosecuted under the Act.

The suspect allegedly received certain virtual assets from an overseas issuer and attempted to sell them at inflated prices on a domestic virtual asset exchange. The suspect reportedly placed large-volume, high-price buy orders and repeatedly submitted fake buy orders using an API (Application Programming Interface) that automatically made order submissions or cancellations under specific conditions. These market manipulation tactics distorted prices and trading volumes, misleading regular users into believing there was significant buying interest in such virtual assets.

The financial authorities concluded their investigation in approximately two months, leveraging their internally-developed large-scale trading data analysis platform and other investigative tools. The prosecution conducted a follow-up investigation under the "Fast Track" process and promptly undertook searches and seizures at seven locations, including the suspect's residence and office.

This landmark case underscores the Act's efficacy and effectiveness in combating unfair practices in the virtual asset industry.

C. Key Takeaways

To ensure the effective implementation of the Act, VASPs in Korea must:

- Continuously enhance their monitoring systems to detect irregular transactions;
- Maintain close collaboration with the financial authorities and investigative agencies; and

- Swiftly identify and systemically respond to covert illegal activities.

It is also crucial for overseas VASPs with operations linked to Korea perform internal reviews to align with Korean regulatory requirements.

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With a dedicated group of professionals who truly understand the technology, business and regulatory climate, Shin & Kim has extensive expertise in assisting clients successfully navigate the rapidly-evolving virtual asset industry in a compliant yet innovative manner.

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