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Self-regulation versus government control in the crypto industry an institutional economics perspective

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Abstract

The rapid development of the cryptocurrency industry has challenged traditional regulatory frameworks worldwide. In Asia, particularly in Japan, regulators have sought to balance innovation with investor protection through hybrid approaches combining state oversight and industry self-regulation. This paper explores the interplay between self-regulation and government control in the crypto sector from the standpoint of institutional economics. It argues that institutional trust, historical path dependency, and market maturity shape the effectiveness of each model and that Japan's experience offers a unique case study of institutional adaptation in the digital economy.

Keywords: Cryptocurrency Regulation; Institutional Economics; Japan; Self-Regulation; Financial Governance; Digital Assets; Asia

1. Introduction

Since the emergence of Bitcoin in 2009, cryptocurrencies have evolved from a niche technology to a significant component of global financial markets. Governments across the world have struggled to design appropriate regulatory responses that foster innovation while mitigating systemic and consumer risks. Nowhere is this tension more visible than in Asia — home to some of the most dynamic crypto markets and diverse regulatory approaches.

Japan stands out as a pioneer. Following the Mt. Gox collapse in 2014, the Japanese government introduced one of the world's first legal frameworks for cryptocurrency exchanges. It recognized Bitcoin as legal property and licensed exchange operators under the Payment Services Act. Importantly, Japan also embraced *self-regulation* through the Japan Virtual Currency Exchange Association (JVCEA), granting it formal recognition as a self-regulatory organization (SRO) in 2018.

This dual system provides a fertile ground to analyze the relationship between self-regulation and government control from an institutional economics perspective.

2. Institutional Economics and the Logic of Regulation

Institutional economics views economic systems as networks of formal and informal rules that govern human behavior. Institutions — including legal norms, cultural practices, and organizational routines — reduce uncertainty and transaction costs by structuring interactions among market participants.

From this perspective, regulation is not merely a legal framework but an *institutional response* to information asymmetries, externalities, and trust deficits. In emerging industries like crypto, where technology outpaces legislation,

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the state may lack the capacity or information to design optimal rules. In such cases, *self-regulation* can serve as a flexible, knowledge-driven mechanism that complements formal law (Black, 2014).

However, self-regulation requires a certain level of institutional maturity — trust, transparency, and accountability — to prevent conflicts of interest or regulatory capture (Braithwaite, 2015). The balance between these forces determines the efficiency of the overall governance model.

3. The Japanese Model: Institutional Evolution and Trust

Japan's approach to crypto regulation illustrates institutional adaptation in action. Historically, Japan has exhibited a strong culture of compliance and a close relationship between industry and regulators, often described as *administrative guidance (gyōsei shidō)* (Okimoto, 2019). This institutional tradition facilitated the development of a cooperative regulatory model.

After the Mt. Gox scandal exposed vulnerabilities in the market, Japanese regulators opted not for prohibition, but for structured legalization. The Financial Services Agency (FSA) (FSA, 2017) mandated exchange registration while delegating certain supervisory functions to the JVCEA — a private body composed of licensed operators. This arrangement institutionalized self-regulation under state oversight, creating a *hybrid governance model* (Evans, 2014).

Empirically, this structure enhanced consumer protection and market legitimacy without stifling innovation. Japan remains one of the few countries where crypto assets are integrated into the financial mainstream, yet operate within a robust regulatory framework.

Japan continues refining its system. In 2020, the PSA and FIEA were amended to include custody and derivatives provisions (FSA, 2020). In 2023–2025, reforms focused on token classification, taxation, and stablecoin issuance (Law.asia, 2025; Cointelegraph, 2025). These updates reflect institutional learning and the integration of self-regulatory mechanisms within formal law.

4. Comparative Insights from Asian Markets

Other Asian economies have taken divergent paths, shaped by different institutional legacies:

- South Korea adopted a more restrictive stance, emphasizing consumer protection and anti-money-laundering compliance, with limited industry self-regulation (Kaur, 2025).
- Singapore pursued a "regulatory sandbox" model under the Monetary Authority of Singapore (MAS), combining flexibility with centralized oversight (MAS, 2020).
- China, conversely, has opted for outright bans on crypto trading and mining, replacing market-driven governance with full state control (Hu, 2024).

These variations demonstrate that regulatory design reflects deeper institutional determinants — such as the level of state capacity, the role of private actors, and the degree of societal trust. Japan's balanced model may thus serve as a reference point for economies seeking a middle path between innovation and control.

5. Discussion: Institutional Trust and the Future of Self-Regulation

From an institutional economics perspective, the success of self-regulation depends on *trust as a public good* (Dasgupta, 2020). When regulators and market actors share information and incentives, self-regulation can lower compliance costs and increase adaptability. Yet, excessive reliance on private governance risks creating "club-like" systems where industry interests override consumer protection.

Japan's FSA–JVCEA framework shows that *embedded autonomy* — where regulators are closely connected to but independent from industry — may represent an optimal institutional equilibrium. For emerging markets, this model underscores the need for transparent governance, professional competence, and mutual trust between public and private institutions.

6. Conclusion

The evolution of crypto regulation in Japan and Asia illustrates a broader truth in institutional economics: effective governance arises not from the dominance of either state or market, but from their strategic interaction. Self-regulation, when embedded within a trusted institutional environment, can complement formal legal structures and enhance regulatory resilience.

As digital assets continue to blur the boundaries between finance and technology, the Japanese experience offers a valuable blueprint. Its institutional synthesis — rooted in cooperation, accountability, and adaptability — may guide other nations navigating the uncertain terrain of crypto governance in the 21st century.

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