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I. Introduction

In March 2018, we have already published a "Swiss Investment Report" on our Wenfei webpage which gives an overview of the Regulatory Treatment of Initial Coin Offerings (ICOs) in Switzerland and Mainland China. Now, this "China Legal Report" is intended to update such previous article and to further deepen the research on the topic "Initial Coin Offerings" by including other Asian countries into the comparison.

II. Comparison on Regulatory Treatment of Initial Coin Offerings

When Bitcoin and many other cryptocurrencies were introduced, they were regarded as decentralized alternatives (i.e. without central authority) to the existing banking system. Will the digital currencies be put through the same regulations as the conventional banking system? How will governments regulate the industry? If they cannot, what alternatives will they consider? What is the effect of their actions on the cryptocurrency markets?

These and other questions will be answered below.

1 Switzerland

The Swiss authorities in general support and welcome the development and implementation of blockchain solutions in the Swiss financial center, even though having possible criminal dangers in mind. Regarding the Regulatory Treatment of ICOs in Switzerland, there have been no regulatory changes since our last publication of the "Swiss Investment Report" in March 2018. Nevertheless, we would like to briefly summarize the regulations in Switzerland once again.

a. Authority

The Swiss Financial Market Supervisory Authority (FINMA) is the responsible authority in Switzerland regarding the handling, control and regulatory treatment of ICOs. FINMA's mission is therefore to protect investors, creditors and policyholders. It also ensures that the financial markets in Switzerland function properly and also publishes information for individuals, issues public warnings and receives substantiated public complaints.

b. Guidance 04/2017

In FINMA Guidance 04/2017, which was published on 29 September 2017, FINMA outlined its position on ICOs and identified areas in which ICOs could fall within the scope of existing financial market regulation. This means, the guidance is no formal law, but a mere

guideline as to which areas of existing Swiss law and in which categories of Swiss law ICOs typically fall.

The Anti-Money Laundering Act applies if the issuance of a token by an ICO provider involves the issuance of a payment instrument. Money laundering risks are especially high in a decentralized blockchain-based system, in which assets can be transferred anonymously and without any regulated intermediaries.

Acceptance of public contributions requires the ICO operator to make a commitment to participants, as the ICO usually requires a banking license.

A licensing obligation for the operation as a securities dealer may exist if the issued tokens are valid as securities (e. g. derivatives).

Moreover, possible links with legislation on collective investment schemes may arise if the assets collected under the ICO are managed externally.

c. Guidelines for enquires regarding the regulatory framework for ICOs

In its still latest ICO Guidelines published on 16 February 2018, FINMA basically explains how it intends to deal with requests from ICO organizers for the applicability of regulations. In addition, the guidelines define the information that FINMA needs in order to deal with such requests and the principles on which it will base its responses.

FINMA categorizes tokens on the basis of their underlying economic function as follows:

• **Payment tokens**: Payment tokens are equivalent to cryptocurrencies and have no further functions or links to other development projects. In some cases, payment tokens can only develop the necessary functionality and can be accepted as means of payment.

For ICOs where the token is to be used as a means of payment and can already be transferred technically on a blockchain infrastructure, FINMA requires compliance with the money laundering regulations. However, FINMA will not treat these tokens as securities.

• **Utility tokens**: Utility tokens are tokens designed to provide digital access to an application or service using a blockchain-based infrastructure.

These tokens shall only qualify as securities if they are solely for the purpose of granting digital access rights to an application or service, and if the utility token can be used in this way at the time of issuance. If a utility token functions exclusively or partly as an investment in economic terms, FINMA treats such tokens as securities. Anti-money laundering regulation is not applicable as long as the main reason for issuing the tokens is to provide access rights to a non-financial application of blockchain technology.

• **Asset tokens**: Asset tokens represent assets such as participations in real physical underlyings, companies or revenue streams or a claim to dividends or interest payments. In

terms of their economic function, the tokens are analogous to equities, bonds or derivatives.

FINMA regards asset tokens as securities, which means that trading in such tokens is subject to the provisions of securities law and the civil law requirements of the Swiss Code of Obligations (e. g. prospectus requirements).

In conclusion, FINMA distinguishes between payment, utility and asset tokens. However, the individual token classifications are not mutually exclusive. Asset and utility tokens can also be classified as payment tokens (called hybrid tokens). From a regulatory point of view, FINMA points out that the anti-money laundering and securities regulations could be relevant. FINMA further clarifies that each project must be decided on its individual merits.

2 Mainland China

In Mainland China, all market participants' financial activities related to ICOs are prohibited in all aspects. According to the latest "*Announcement on Preventing Token Fundraising Risks*" (hereinafter referred to as "Announcement") of 4 September 2017 jointly published by the People's Bank of China, the Office of the Central Leading Group for Cyberspace Affairs, the Ministry of Industry and Information Technology, the State Administration for Industry and Commerce, the China Banking Regulatory Commission, the China Securities Regulatory Commission and the China Insurance Regulatory Commission, tokens or "virtual currencies" used in the ICOs financing are not issued by competent authorities, do not have money attributes such as legal compensation and compulsory nature, have no equal legal status with currencies, and thus should not be circulated and used in the market as currencies.

Thus, all fundraising activities through token issuance shall stop immediately from the date of the Announcement. In particular, the Announcement states the following:

• **Organizations and individuals** who have already raised money through token fundraising should provide refunds or make other arrangements to reasonably protect the rights and interests of investors and properly handle risks.

• **Regarding token trading platforms**, the financial administration authority shall request the telecommunication authority to close down its website platform and mobile App, request the cybersecurity authority to remove its mobile App from app stores, and request the commercial and industrial authority to revoke its business license.

• **Financial institutions and non-banking payment institutions** shall promptly report to relevant authorities if they spot any violation of ICO fundraising and trading.

• **Chinese financial industry associations** are obliged to urge their members to voluntary resist illegal financing activities relating to ICOs.

• Chinese authorities also alert publicly the potential risks of ICOs, which includes the risk of false assets, the risk of business failure and the risk of investment and speculation, and even encourage the **public** to promptly report relevant violation clues.

On 24 August 2018, the Banking Regulatory Commission, the Central Network Information Office, the Ministry of Public Security, the People's Bank of China and the General Administration of Market Supervision published a *Warning about Preventing Illegal Fundraising in the Name of "Virtual Currency" and "Blockchain".* The warning emphasizes that the general public should be rational about blockchain, should not blindly believe, should establish a correct monetary concept and investment philosophy, should effectively raise the awareness of risk and actively report the violations of the law to the relevant departments.

3 Hong Kong

a. Authority

Already in the past, the Securities and Futures Commission (SFC), which is the responsible financial watchdog in Hong Kong, has issued a number of circulars clarifying its regulatory stance on virtual assets.[1] Under existing regulatory remits in Hong Kong, if the virtual asset falls under the legal definition of "securities" or "futures contracts" (or equivalent financial instruments), it enjoys the protections afforded under the "*Securities and Futures Ordinance*" (SFO). The SFC also reminded intermediaries in a circular dated 1 June 2018 about the notification requirements, namely licensing and registration, if they intend to provide trading and asset management services involving crypto-assets. However, many virtual assets do not amount to "securities" or "futures contracts".

On 1 November 2018, the SFC issued a comprehensive set of regulations with immediate effect governing cryptocurrencies in a move to enhance investor protection, which analysts believe could help make the city a major trading center for virtual assets. The SFC

[1] These include the Statement on initial coin offerings dated 5 September 2017, Circular to Licensed Corporations and Registered Institutions on Bitcoin futures contracts and cryptocurrency-related investment products dated 11 December 2017, and the press release, "SFC warns of cryptocurrency risks", dated 9 February 2018.

in particular unveiled two Circulars, one is the "*Statement on regulatory framework for virtual asset portfolios managers, fund distributors and trading platform operators*" (hereinafter referred to as "Circular 1") and the other one is on the "Distribution of virtual asset funds" (hereinafter referred to as "Circular 2").

b. Circular 1 with Annex

Circular 1 describes the unique features and characteristics of virtual assets and outlines some of the risks associated with investing in them.

The SFC has developed a set of standard terms and conditions which captures the essence of the Existing Requirements, adapted as needed to better address the risks associated with virtual assets. For instance, **only professional investors** as defined under the SFO should be allowed to invest in any virtual asset portfolios, namely the ones with at least HKD 8 million in investment assets and two years of experience.

Moreover, licensed corporations with an intention to **invest 10% or more of the gross asset value (GAV)** of the portfolio in virtual assets will need to be licensed by the SFC.

Separately, the SFC also sets out a conceptual framework for the potential regulation of **virtual asset trading platforms**. In particular, such platforms need to join the **SFC Regulatory Sandbox** under which they can continue to trade while negotiating on the licensing requirements. However, it is uncertain how long the sandbox period shall last.

c. Circular 2

Circular 2 reminds intermediaries licensed or registered for dealing in securities or asset management, which are engaged in distributing virtual asset funds under their management, about the existing regulatory requirements and provides guidance on the expected standards and practices in relation to the distribution of virtual asset funds. They are also reminded that any failure to implement adequate systems and controls to ensure compliance with the requirements mentioned in Circular 2, before they engage in the distribution of virtual asset funds, may affect their fitness and properness to remain licensed or registered and may result in disciplinary action by the SFC.

The new rules definitely close a regulatory loophole. It will be seen if they will also attract more mainlanders or other investors to trade cryptocurrency assets in Hong Kong.

4 Singapore

Similar to Switzerland, Singapore has taken a rather progressive approach to regulation of cryptocurrency and ICOs. Consequently, many ICOs are registered in Singapore. On July 26, 2018, a Korean team called MVL introduced Tada, an equivalent of "Uber" on the

blockchain, in Singapore. Tada is an on-demand car sharing service that utilizes MVL's technology. The Tada app is built on MVL's blockchain ecosystem.

Like Hong Kong, Singapore also provides fintech regulatory sandboxes.

a. Authority

The Monetary Authority of Singapore (MAS) is the central bank and financial regulatory authority and administers the various statutes pertaining to money, banking, insurance, securities and the financial sector in general, as well as currency issuance. Like FINMA in Switzerland, MAS also points out that digital tokens that perform functions which may not be within MAS' regulatory purview may nonetheless be subject to other legislation for combating money laundering and terrorism financing.

b. A Guide to Digital Token Offerings ("Guide")

On 14 November 2017, MAS has specifically issued a guideline to digital token offerings, which illustrates the application of securities laws to digital token offerings and issuances. The securities laws refer to the Securities and Futures Act ("SFA") and the Financial Advisers Act ("FAA").

The Guide, inter alia, emphasizes on the following aspects:

• Cryptocurrency exchanges which allow the exchange of any token constituting "capital markets products" regulated under the SFA need to seek **MAS's approval, recognition or exemption under the SFA**. Under section 2(1) of the SFA, capital markets products include any securities, futures contracts and contracts or arrangements for purposes of leveraged foreign exchange trading and such other products as MAS may prescribe as capital markets products.

• A person may only make an offer of digital tokens which constitute securities ("Offer"), if the Offer complies with the requirements under Part XIII of the SFA. This includes the requirements that the Offer must be made in or accompanied by a **prospectus** that is prepared in accordance with the SFA and is registered with MAS ("Prospectus Requirements").

• An Offer may nevertheless **be exempt** from the Prospectus Requirements where, amongst others –

(i) the Offer is a small offer of securities of an entity, that does not exceed S$5 million (or its equivalent in a foreign currency) within any 12-month period, subject to certain conditions;

(ii) the Offer is a private placement offer made to no more than 50 persons within any 12-month period, subject to certain conditions;

(iii) the Offer is made to institutional investors only; or

(iv) the Offer is made to accredited investors, subject to certain conditions.

• A person who provides any financial advice in respect of any digital token that is an investment product, must be authorized to do so by a **financial adviser's license**, or be an exempt financial adviser, under the FAA.

• A person who establishes or operates a **trading platform** in Singapore in relation to digital tokens which constitute securities or futures contracts, must be approved by MAS as an approved exchange or recognized by MAS as a recognized market operator under the SFA, unless otherwise exempted.

Cryptocurrency exchanges that do not allow trading of any capital markets products regulated under the SFA are currently not subject to regulation in Singapore.

5 Summary

	Switzerland	Mainland China	Hong Kong	Singapore
Cryptocurrency exchange legal	YES	NO	YES	YES
Responsible authority	FINMA	No special authority	SFC	MAS
Cryptocurrencies as legal tender	YES	NO	NO	NO
Registration required	YES	N/A	YES	YES

III. Conclusion

In 2017, the United States were the number one market for ICO issuance based on the number of funds raised, followed by Switzerland and Singapore.

Singapore historically has been a financial hub in Southeast Asia and now has also gradually become the crypto hub of Asia. Compared to the rest of Asia and the rest of the world, the regulators in Singapore are well-informed and relatively transparent about their views on blockchain and cryptocurrency. However, Switzerland might still be the most crypto-friendly country in the world, whereas Mainland China is probably among the strictest countries. It will be seen if Hong Kong`s first set of rules issued on 1 November 2018 (Circular 1 and 2) could help turn Hong Kong into a major cryptocurrency hub, as expected by analysts.

Such as Tada in Singapore, Didi, China's well-known ride-sharing company, has also looked to build out its own blockchain-based ride-sharing program, called VV Go, which seeks to

improve passenger safety and increase the income of drivers. VV Go's launch is still pending up to now, and its home is intended to be in Toronto, Singapore, Hong Kong or San Francisco. It will be seen which country will best fulfill Didi`s requirements.

It should be noted that none of the abovementioned states so far has enacted a specific legal act regarding the treatment of ICOs. They rather issued mere guidelines which are not legally binding. However, these guidelines provide the way on how ICOs are to be treated legally and factually, particularly how ICOs fit into the existing legal regime.

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