

A Global Regulatory Overview of Token Offerings

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A VARIED WORLD VIEW

The world's attitude toward token offerings, sales and issuances is ever-shifting. The positions of various countries range from an official recognition of no interference to a full ban on digital currencies. Many nations are pursuing changes to their regulatory policies to keep pace with broad market interest in cryptocurrencies and other digital assets. This article summarizes recent developments by lawmakers and regulatory authorities in certain key jurisdictions around the globe (other than the United States, which is the subject of a separate article [Payment Systems and Electronic Fund Transfers Guide 100:800] and the related impact on the market for cryptocurrencies and other digital assets. The regulations and guidance noted in this article are applicable only with the specified jurisdiction. Consequently, global or multi-jurisdictional offerings or sales of tokens must take into account the local law of each jurisdiction in which the tokens are being offered, sold or otherwise distributed.

The G20 countries participate in an intergovernmental Financial Action Task Force (FATF), which has set the global standards for anti-money laundering, among other topics. In an April 2019 report to the G20, FATF proposed standards on digital assets and cryptocurrencies, including a risk-based approach to supervision and monitoring. Increasing pressure is building from G20 countries for unified cryptocurrency regulatory standards globally and a progress report is expected to be delivered at the June 2019 G20 meeting in Japan.

SWITZERLAND

Regulators in Switzerland have been active in the development of the cryptocurrency for the past several years. Switzerland has been at the forefront of favored jurisdictions by many issuers and market participants because of its fintech-friendly regulatory environment. The Swiss foundation structure has been widely used by many global digital asset developers, including Ethereum, as a way to minimize or avoid compliance with securities law regimes in other jurisdictions. Whether this is effective needs to be evaluated on a case-by-case basis, as it is unwise to make broad statements that certain rules in other jurisdictions would not be applicable under a foundation-type structure.

Offerings of digital assets under Swiss law are subject to a number of financial market acts, notably including: the Banking Act and related Ordinance, which govern licensing requirements relating to public contributions; the Federal Intermediated Securities Act, the Stock Exchange Act and related Ordinance, the Financial Market Infrastructure Act and related Ordinance, the Code of Obligations, and the Anti-Money Laundering Act. The Swiss Financial Market Supervisory Authority, or FINMA, issued a guidance note on the regulatory treatment of token offerings in April 2017, and on February 16, 2018 published ICO Guidelines (<https://www.finma.ch/en/documentation/finma-guidance/>).

Although there are no specific regulations in Switzerland addressing digital assets, the ICO Guidelines were designed to facilitate discussions with issuers and other market participants as to the expected application of the various financial market regulations to this evolving asset class and related transactions in initial offers and sales, as well as secondary trading.

The ICO Guidelines set out four categories of tokens: payment tokens, utility tokens, asset tokens (including derivatives) and pre-sale tokens. The latter two categories will generally be treated by FINMA as securities. Payment tokens, such as Bitcoin and Ether, are not considered securities if the token is designed to act principally as a means of payment or barter. Similarly, utility tokens would not be considered securities if they confer digital rights to an application or service and are, in fact, useable on the respective platform or application. If there is an investment purpose associated with the utility token, the characterization of the token is likely to be changed by FINMA to that of a security.

SINGAPORE

Singapore has also emerged as a favored jurisdiction for offers and sales of digital assets. On August 1, 2017, the Monetary Authority of Singapore (MAS) clarified that if a digital token constitutes a capital market product regulated under the securities laws administered by MAS, the offer or issue of the digital tokens must comply with applicable securities laws, specifically the Securities and Futures Act (Cap. 289) (SFA) and the Financial Advisors Act (Cap. 110) (FAA). Section 2(1) of the SFA defines a "capital market products" as any securities, futures contracts, contracts or arrangements

for the purposes of foreign exchange trading, contracts or arrangements for the purposes of leveraged foreign exchange trading. Consequently, a digital token may constitute a share, a debenture or a unit in a collective investment scheme. An offer of a digital token that constitutes a security or a unit must comply with the SFA, including the prospectus requirements, or otherwise be exempt from the prospectus requirements. Exemptions are available if the offer (i) does not exceed \$5 million (or the foreign currency equivalent) within any 12-month period, subject to certain exceptions; (ii) is a private placement to not more than 50 persons within any 12-month period, subject to certain exceptions; (iii) is made only to institutional investors; or (iv) is made only to accredited investors, subject to certain exceptions. The guidance offered by the MAS includes a series of case studies to assist market participants in the analysis of the application of Singapore law to various digital token transactions.

In addition, persons operating a primary trading platform in Singapore for digital tokens which constitute any type of capital markets products may be conducting a regulated activity under the SFA. In such a case, the person must hold a capital markets services license for that regulated activity unless otherwise exempt. Similarly, persons providing financial advice in respect of any digital token that is an investment product must be authorized and licensed (or otherwise be exempt) under the FAA.

On January 24, 2019, the MAS issued a notice that it had halted a securities token offering in Singapore for the issuer's failure to fully comply with SFA regulatory requirements. The issuer had intended to rely upon an exemption from registration under the SFA, which requires compliance with certain conditions, including a requirement not to advertise the offer. The issuer's legal advisors put out a LinkedIn post calling attention to the offer.

MALTA

Malta has sought to become a global hub for fintech and related products and services in recent months and has successfully been attracting blockchain and cryptocurrency enterprises to its jurisdiction. During 2018, the Malta Financial Services Authority (MFSA) has been active in developing a comprehensive set of regulations to facilitate international token offerings through the use of a Maltese-organized entity. The Malta Digital Innovation Authority (MDIA) was established in July 2018 as a new regulatory authority to regulate and develop a framework for innovation, including distributed ledger technology, blockchain, and smart contracts and certifying service providers and technology arrangements with respect to digital assets. Two additional laws, the Innovative Technology Arrangements and Services Act (ITAS) and The Virtual Financial Asset Act (VFAA), came into effect on November 1, 2018. The ITAS provides for the regulation of designated innovative technology arrangements and will work in parallel with the MDIA. The

VFAA regulates the issuance of tokens in or from Malta, the operation of digital asset exchanges and the provision of digital asset-related services.

EUROPEAN UNION

On November 13, 2017, the European Securities and Markets Authority (ESMA) issued a Statement (<https://www.esma.europa.eu/>), alerting investors to the high risks associated with initial coin offerings (ICOs), highlighting concerns about fraud, the high risk of loss of one's investment, extreme price volatility, inadequacy of information and flaws in the technology. Although the European Union (EU) generally has permitted token offerings to proceed, subject to adherence to Anti-Money Laundering/Know Your Customer (AML/KYC) policies and to the required business regulations and licenses, on October 8, 2018, the chair of ESMA stated that ESMA was examining whether ICOs should be regulated as securities offerings, either through new regulations or through compliance with existing rules. A report is expected by the end of 2018 or early 2019. ESMA's 2019 Annual Work Programme (<https://www.esma.europa.eu/>) includes €1 million to monitor activities in cryptocurrencies during 2019 and has an overall objective of achieving a coordinated approach to the regulation and supervisory treatment of new or innovative financial activities, including digital assets.

On January 9, 2019, EMSA published a guidance document entitled "Advice on Initial Coin Offerings and Crypto-Assets." The Advice sets out EMSA's position on issues relating to crypto-assets that qualify as financial instruments under MiFID, along with associated risks when such assets do not so qualify. For qualifying instruments, EMSA notes that there are areas within the existing regulatory framework that require potential reconsideration of the requirements to allow for effective application of the existing regulations. For non-qualifying instruments, EMSA believe that anti-money laundering requirements should apply to all crypto-assets and activities involving such assets.

UNITED KINGDOM

Cryptocurrencies and related assets are not currently regulated by The Financial Conduct Authority (FCA) in the United Kingdom, provided they are not part of other regulated products or services. The FCA has stated that it will evaluate token offerings on a case-by-case basis to determine if a particular offering or issuance falls within the existing regulatory regime. Cryptocurrency derivatives are considered by the FCA to fall within the category of financial instruments regulated under the Markets in Financial Instruments Directive II (MFID II), but are not currencies or commodities for regulatory purposes of that Directive.

In August 2018, the FCA announced the creation of the Global Financial Innovation Network (GFIN) in collaboration with 11 financial regulators and organizations to create a global

“sandbox” for discussion and development of policies relating to ICOS, distributed ledger technology and other emerging technologies, along with related AML/KYC concerns (<https://www.fca.org.uk/publications/consultation-papers/global-financial-innovation-network>).

In January 2019, the FCA published Consultation Paper (CP19/3) available <https://www.fca.org.uk/publication/consultation/cp19-03.pdf>, entitled “Guidance on Cryptoassets.” The Guidance is intended to clarify what activities and products fall under FCA regulation. In particular, tokens with characteristics similar to traditional financial instruments, such as shares, debentures or units would be defined as “security tokens” and fall with the regulated regime. “Utility” and “exchange” tokens, by contrast, provide access to current or prospective products or services, utility tokens often granting rights akin to pre-payment vouchers or coupons. According to the FCA, ICOs that issue utility tokens would not be subject to regulation as financial instruments in the UK (but could be subject to e-money regulations).

FRANCE

On April 11, 2019, the French Parliament adopted the “Action Plan for Business Growth and Transformation (Pacte)”, which established a new legal framework for providers of digital asset services, as well as ICOs. The new law also strengthens the powers of France’s Financial Markets Authority (AMF) as the principal regulatory for the digital asset and cryptocurrency industry in France. Under the Pacte, providers of digital asset custody services and exchange/trading services with third parties are subject to mandatory registration with the AMF. Capital raising activities, however, using digital assets is legal in France and no AMF approval is required unless an issuer is seeking to solicit the general public. ICOs without approval or that employ the services of unlicensed service providers are prohibited from solicitation and sponsorship activities.

CANADA

The Canadian Securities Administrators (CSA) stated in August 2017 that many offers and sales of digital assets constitute the sale of securities and may also involve derivatives, which in each case are subject to existing Canadian securities laws and regulatory authorities. The 2017 statement by the CSA notes that, in the case of security tokens or coins, businesses will be expected to comply with existing prospectus requirements or otherwise proceed in reliance on an available exemption from the regulatory regime. Businesses trading in these digital assets must also comply with broker-dealer registration requirements or rely upon an exemption from the registration requirement. Similarly, cryptocurrency investment funds in Canada are expected to comply with custodial and other requirements.

The CSA clarified its position in June 2018 on when an offering of tokens may constitute an offering of securities

(2018 Notice). In particular, the CSA noted that a distribution of securities may occur where the offering involving the distribution of an investment contract, and/or the offering and/or the tokens issued are securities under one or more of the other enumerated definitions of a securities. The definition of “investment contract” under Canadian law relies upon the Supreme Court of Canada’s 1978 decision in Pacific Coast Coin Exchange and its progeny: an investment of money, in a common enterprise, with the expectation of profit, derived significantly from the efforts of others. The 2018 Notice sets out a number of examples of token offerings where one or more of the elements of an investment contract are present, and the possible implications for how it might be treated within the current regulatory regime, including multiple step structures utilizing a SAFT, or simple agreement for future tokens. The 2018 Notice alerts market participants that the CSA may consider a token delivered at the second or later step in a SAFT transaction as a security, despite the fact that the token may have some utility. This is consistent with the current view of the U.S. Securities and Exchange Commission.

Cryptocurrency exchanges that operate in Canada and offer security token/coins must determine if the exchange constitutes a “marketplace” under applicable provincial law. Marketplaces are required to comply with the rules governing exchanges or alternative trading systems. An exchange doing business in Canada must apply to the applicable securities regulatory authority for recognition or seek an exemption.

Cryptocurrencies are recognized as intangible assets and it is expected that commercial dealers will need to be registered and regulated as money service businesses. During the course of 2018, a number of major Canadian banks have imposed bans on digital currency transactions, including through the use of credit cards.

The CSA has developed a “Regulatory Sandbox” for the purpose of regulating fintech projects that would not normally fit in the national regulatory scheme, such as ICOs. It also allows businesses to register and/or obtain exemptive relief from securities law requirements in order to test their products, services and applications throughout the Canadian market on a time-limited basis.

AUSTRALIA

In May 2018, the Australian Securities and Investments Commission (ASIC) issued an Information Sheet (<https://asic.gov.au/regulatory-resources/digital-transformation/initial-coin-offerings-and-crypto-currency/#what>) to provide market participants with guidance on the potential application of the Corporations Act 2001 (2001 Act) to entities considering raising funds through an ICO and to other cryptocurrency or digital token businesses. ASIC clarified that the 2001 Act applies to ICOs and digital assets that are “financial products” and that a token described as a “utility” does not mean it is not a financial product.

Consequently, issuers and promoters must comply with the registration and prospectus delivery requirements, unless an exemption is otherwise available. Financial products include managed investment schemes, shares, derivatives, or a non-cash payment facility. Operating an exchange for a financial product in Australia requires the platform operator to hold an Australian market license, unless the operator is otherwise covered by an exemption.

TAIWAN

In October 2018, the Taiwan Financial Supervisory Commission (FSC) announced that it will introduce a legal framework for token offerings. According to FSC Chairman Wellington Koo, the regulations aim to combat the fraud that has become commonplace in the industry, and will enable ICOs to become “as liquid and safe as retail stocks.” Koo has also stated that there will be exemptions for tokens and currencies that are used as a means of exchange at certain establishments and retailers, such as airlines and supermarkets. Additionally, the FSC is in the process of developing a review process as well as defining what types of ICOs will be eligible for issuance. The regulations are expected to be in place by June 2019.

However, Taiwan’s Securities and Futures Bureau Director-General, Tsai Li-ling, has stated that the ICO regulations will be separate from current regulations that deal with the trading of cryptocurrencies. Overall, the goal of Taiwanese regulations is not to create roadblocks that stop the progress of the blockchain industry which is becoming more widely accepted in that country.

In November 2018, the Legislative Yuan, one of Taiwan’s five branches of government, adopted the “Money Laundering Control Act and Terrorism Financing Prevention Act. Significantly, the Act gave the FSC authority over cryptocurrency exchanges, including the ability to ban transactions suspected of being tied to fraudulent operations. This move has fueled speculation that Taiwan will now proceed to adopt local rules to regulate cryptocurrency and blockchain activities within its borders.

THE UNITED ARAB EMIRATES

In September 2018, the United Arab Emirates’ (UAE) Securities and Commodities Authority (SCA) approved a plan to regulate token offerings and recognize them as securities. The decision, which represents a departure from the SCA’s prior pronouncements that it would not regulate ICO activity, came after the SCA reviewed a study on best international practices, and includes a set of mechanisms as part of an integrated project to regulate digital securities and commodities. The SCA is drafting regulations for ICOs with international advisers and is working with the Abu Dhabi and Dubai stock markets to develop trading platforms for the offers. The SCA plans to have regulations in place during the

first half of 2019. It is unclear whether all digital assets will be treated as securities.

Bahrain On February 25, 2019, Bahrain’s central bank announced that it had issued final rules relating to crypto assets, including licensing and governance, as well as cybersecurity. The central bank’s action is designed to support the development of comprehensive rules for a fintech ecosystem supporting Bahrain’s leading position as a financial hub in the Middle East and North Africa. The central bank has established an incubator-style sandbox licensing program, including cryptocurrency exchange platforms and blockchain companies.

AUSTRIA

In October 2018, the Austrian Financial Market Authority (*Finanzmarkt-aufsicht, FMA*) published guidelines (<https://www.fma.gv.at/en/cross-sectoral-topics/fintech-navigator/initial-coin-offering/>) on how it views ICOs from a financial services regulatory perspective. The guidelines are available on the FMA’s FinTech Navigator, currently in German only, and intend to provide clarification on the FMA’s view on “Crypto Assets,” the term that the FMA uses for virtual currencies, coins and tokens.

The FMA’s definition of a typical ICO is in line with other regulators around the globe, and its regulatory approach is also similar. In line with market practice, the FMA distinguishes broadly (and without prejudice) between the following three basic categories of tokens: (i) security / investment token, (ii) payment / currency token, and (iii) utility token.

Because ICOs can be structured in very different manners, regulatory aspects need to be assessed on a case-by-case basis. In its guidelines, the FMA has provided a comprehensive overview of potential regulatory areas that need to be analyzed before launching an ICO:

- ICOs may trigger licensing requirements under the Austrian Banking Act, e.g. taking deposits, issuing means of payment, underwriting or holding securities for third parties.
- Coins or tokens issued in an ICO may qualify as transferable securities within the meaning of European securities legislation such as MiFID2. In such a case, services rendered in relation to an ICO may require a respective investment firm license.
- An offering of tokens that qualify as transferable securities or investments (*Veranlagungen*; a local Austrian securities law concept) may require a prospectus pursuant to the Austrian Capital Markets Act.
- Crypto assets that perform a payment function may fall under the scope of the Payment Services Act implementing PSD2.

- An ICO may also fall in the scope of the Alternative Investment Fund Managers Act, in particular if Crypto Assets raised are used for investment for the benefit of their holders in accordance with a predefined investment strategy (in that respect, the FMA has previously also mentioned that raising funds for Bitcoin mining also qualifies as funds raised for investment).
- Lastly, the FMA has clarified that services provided in the course of an ICO may also trigger applicable Know-Your-Customer / Anti-Money Laundering requirements, for example, in connection with the provision of wallet services and token exchanges.

RUSSIA

In October 2018, Russia's Federal Financial Monitoring Service announced that it would regulate cryptocurrency-related transactions in the country in accordance with recommendations issued by the Financial Action Task Force. Rosfinmonitoring, the Russian regulator, will register, license and monitor cryptocurrency exchanges, crowdfunding platforms and providers of wallet services for digital assets. The financial authority intends to regulate exchanges and trading for cryptocurrencies and digital assets, as well as fiat money. It is expected that a minimum threshold will be established for regulatory action.

On March 28, 2018, a draft bill intended to regulate cryptocurrencies, ICOs and crypto mining was introduced in the Duma, the lower house of the Russian parliament. The draft bill has been revised a number of times, including to remove references to cryptocurrencies and crypto mining, and alternative measures have been proposed to give cryptocurrencies special status in the country. The future of these legislations are subject to significant uncertainty.

ISRAEL

On May 20, 2019, an Israeli central district court ruled in favor of the Israeli Tax Authority and recognized Bitcoin as a financial asset and not as a currency. The implications for this ruling are that profits from the sale of Bitcoin in Israel would be subject to capital gains tax, which is 25%–30% in Israel. The court noted that, although the status of Bitcoin had yet to be clarified under Israeli law, it did not consider Bitcoin a currency for tax purposes. The court accepted the Israeli Tax Authority's position that currency should be defined by the country's central bank, which definition does not currently extend to cryptocurrencies. The ruling applies retroactively and is expected to apply to all cryptocurrency-related profits.

INDIA

A regulatory framework is being finalized by the Department of Economic Affairs in India in response to a proposed bill

introduced in April 2019 called "Banning of Cryptocurrencies and Regulation of Official Digital Currencies Bill 2019." The bill was circulated to different government agencies for review and comment, including the Department of Economic Affairs, the Central Board of Direct Taxes, the Central Board of Indirect Taxes and Customs, and the Investor Education and Protection Fund Authority. The bill proposes to ban sales, purchases and issuances of all cryptocurrencies in India. It is expected that review and action on the bill could take up to six months or longer. The details of the bill had not been made public as of May 2019.

CHINA AND OTHER COUNTRIES THAT HAVE BANNED ICO ACTIVITY

China, which was once the largest market for trading cryptocurrencies, has taken a particularly harsh stance. Chinese government regulators view cryptocurrencies as a threat to its own national currencies CNY, and in 2017, the country banned ICOs. The group of regulators that issued the ban provided a list of 60 major ICO platforms for local financial watchdogs to inspect. That same year, China's biggest cryptocurrency exchanges halted trading for domestic customers at the behest of the government. At the beginning of 2018, China moved to block foreign trading platforms operating in China.

In November 2018, the People Bank of China (PBoC) announced it had widened its regulatory scrutiny to include token airdrops, which it characterized as "disguised" ICOs.

ICO exchanges cannot operate in China and their websites are blocked. Consequently, many big exchanges have migrated out of the country. Some financial analysts believe China would be open to blockchain or cryptocurrency development if it were manageable.

In December 2018, China's Municipal Bureau of Finance announced that security token fundraising is illegal and stated its intent to ban airdrops. In January 2019, the Cyberspace Administration of China announced regulations requiring all companies utilizing blockchain technology to adhere to anti-anonymity regulations. The new regulations came into effect on February 15, 2019.

In addition to China, the following countries have banned (as of the date of publication of this article) cryptocurrencies, including consulting, ICO investing, buying, selling or trading bitcoin or any other token:

- Bangladesh
- Nepal
- Macedonia
- Bolivia

- Ecuador
- Pakistan
- Algeria
- Morocco

Regulation is constantly evolving and market participants must confirm the status of current regulation in each jurisdiction in which a token offering or related issuance or trading activities is anticipated.

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