

## Twice In Two Days: China and Hong Kong Weigh In On Token Sales

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Twice in as many days, powerhouse jurisdictions in Asia have weighed in on token sales. **China has halted them altogether**, while **Hong Kong** has, in many ways, followed the path tread recently by the United States, Singapore and Canada, announcing that certain tokens may be securities. [1] Given token sales' global reach, many, **including the author and her colleagues**, have predicted that more and more jurisdictions would provide guidance concerning token sales and that such guidance may, in some ways, be consistent with the SEC's statements and acknowledgement that certain tokens may be securities. [2] The more jurisdictions around the world that weigh in on token sales and provide legal guidance, the fewer and fewer places would-be fraudsters and scam artists will be able to launch deceptive or fraudulent token sales. From that perspective, the **Chinese ban on token sales** and the **announcement this week by Hong Kong** may, in some ways, be viewed as a way to clear the path for those issuers that wish to launch legally compliant and responsible token sales. As nations around the globe weigh in and provide legal guidance concerning token sales, a more legitimate, responsible and sustainable token sale market may emerge.

Below are some thoughts regarding the Chinese and Hong Kong guidance, respectively:

### ***Bull in a China Shop? China Reportedly Halts Token Sales and Will Investigate Prior Chinese Token Launches***

This year, token sales have been a big business in China, with Chinese media outlets reportedly stating in July that over US \$397 million in the aggregate had been raised from 65 token sales, as reported by **CNBC**. [3] On September 4, 2017, the Chinese government **reportedly put a halt to token sales** and announced that it **will be investigating certain token sales that launched previously**. [4]

Over the prior week or so, there had been **rumblings on the Internet** and elsewhere that Chinese regulators were looking closely at token sales and that the National Internet Finance Association of China had expressed concerns regarding fraudulent and misleading sales tactics, as well as sales of tokens that arguably were securities without complying with applicable securities laws. [5] On August 31, 2016, Duncan Riley **reported** "China's Securities and Futures Commission, the China Banking Regulatory Commission and other regulators have held a number of meetings to discuss 'appropriate regulatory measures.' Those measures are said to include controls on how much an ICO can raise, regulations pertaining to information disclosure, supervision of ICOs and compulsory investment risk disclosure. The report adds that if ICOs are found to be considered too risky across the board, they make [sic] consider banning all ICOs outright until the concerns were addressed." [6] **Reports earlier this week that the Chinese government will require token issuers to return money to investors** follow recent news in the United States regarding the **SEC reportedly having contacted token issuer Protostarr**, leading to the shutdown of the Protostarr token sale. [7]

While this author cannot speak or read Chinese and, accordingly, is reliant on media reports, the message from China – that some token sales may be sales of securities, that investors need to be wary of fraudsters and bad actors, and that token sales are not somehow exempt from the need to consider and comply with regulatory frameworks and laws – sounds

somewhat consistent with the messages that the United States Securities and Exchange Commission (the "SEC"), the Canadian Securities Administrators (the "CSA") and the Monetary Authority of Singapore (the "MAS") recently have released. Although China appears to have taken an additional step to ban token sales [8] – at least for the time being – while the U.S., Canada and Singapore have not done so, China's actions this week may be an example of another government trying to understand, regulate and educate the public of the risks involved in this new form of capital raising.

It is interesting to consider whether the Chinese token sale stoppage will be a permanent one. A moving target often is more difficult to hit, and it is worth considering whether the Chinese government may be "pressing pause" on token sales in order to explore ways to assess and regulate future token sales, rather than issuing a permanent ban on all token sales. Perhaps this may lead to the maturation and development in China of legally compliant token sales under applicable law.

### ***Hong Kong Joins the Pack: Certain Tokens May Be Securities***

On September 5, 2017, Hong Kong made clear that certain tokens may be securities. [9] In its release, Hong Kong's Securities and Futures Commission (SFC) stated that it "has noticed an increase in the use of initial coin offerings (ICOs) to raise funds in Hong Kong and elsewhere. This statement serves to explain that, depending on the facts and circumstances of an ICO, digital tokens that are offered or sold may be "securities" as defined in the Securities and Futures Ordinance (SFO), and subject to the securities laws of Hong Kong." [10]

Explaining that, when a given digital token constitutes a "security" (a category that the SFC mentions includes debentures, interests in a collective investment scheme and shares) under Hong Kong law, dealing in or advising in connection with such token, or managing or marketing a fund that invests in such token, "may constitute a 'regulated activity'.... Parties engaging in a 'regulated activity' are required to be licensed by or registered with the SFC irrespective of whether the parties involved are located in Hong Kong, so long as such business activities target the Hong Kong public." [11]

In addition, the SFC sent a warning to token issuers, secondary traders of tokens and cryptocurrency exchanges that securities laws and other legal requirements may apply to them, including requirements for certain registrations and authorizations (unless an exemption applies). Among other things, the SFC stated: "Parties engaging in the secondary trading of such tokens (eg, on cryptocurrency exchanges) may also be subject to the SFC's licensing and conduct requirements. Certain requirements relating to automated trading services and recognised exchange companies may be applicable to the business activities of cryptocurrency exchanges." [12]

The SFC ended its release by cautioning potential investors regarding the possibility of fraud, significant investment risks and potential lack of liquidity, but not before reminding issuers of anti-money laundering and similar matters. Noting that tokens issued in token sales may be transacted or held on an anonymous basis, the SFC stated that "inherent and significant money laundering and terrorist financing risks" exist and referenced its January 16, 2014 circular reminding licensed corporations and associated entities "to take all reasonable measures to ensure that proper safeguards exist to mitigate these risks." [13]

### ***Key Takeaways***

While it is unclear which jurisdiction will be the next one to speak out about token sales, many issuers are beginning to realize that no token sale is an island, so to speak. If an issuer is marketing, offering or selling digital tokens into a jurisdiction, ignorance of that jurisdiction's laws does not mean that laws do not apply. A new token sale era arguably is beginning.

[1] <https://www.linkedin.com/pulse/sec-issues-investor-alert-warn-investors-ico-related-klayman-kuzar>, <https://www.investor.gov/additional-resources/news-alerts/alerts-bulletins/investor-alert-public-companies-making-ico-related>, <https://www.mofo.com/resources/publications/170726-howey-got-here-sec-token-offerings.html>, <https://www.sec.gov/litigation/investreport/34-81207.pdf>, <https://www.mofo.com/resources/publications/170802-singapore-token-offerings.html>, <http://www.mas.gov.sg/news-and-publications/media-releases/2014/mas-to-regulate-virtual-currency-intermediaries-for-money-laundering-and-terrorist-financing-risks.aspx>, [http://www.osc.gov.on.ca/en/SecuritiesLaw\\_csa\\_20170824\\_cryptocurrency-offerings.htm](http://www.osc.gov.on.ca/en/SecuritiesLaw_csa_20170824_cryptocurrency-offerings.htm), <http://bloombergtv.ca/shows/bloomberg-markets-canada/bloomberg-markets-canada-episode/?epid=828&sgid=6>, <https://www.linkedin.com/pulse/bull-china-shop-reportedly-halts-token-sales-prior-klayman-kuzar>

[2] <https://www.blockchaintechnews.com/articles/attorneys-offer-perspective-on-sec-ruling/>

[3] <https://www.cnbc.com/2017/08/31/new-cryptocurrencies-and-icos-create-financial-risk-says-chinas-national-internet-finance-association.html>

[4] <http://www.atimes.com/article/60-ico-token-distribution-platforms-face-investigation/>, <https://siliconangle.com/blog/2017/09/03/china-bans-initial-coin-offerings-pending-review>, <http://fortune.com/2017/09/04/ico-china-central-bank-ban/>

[5] <https://siliconangle.com/blog/2017/08/31/chinese-regulators-consider-massive-crackdown-initial-coin-offerings/>

[6] <https://siliconangle.com/blog/2017/08/31/chinese-regulators-consider-massive-crackdown-initial-coin-offerings/>

[7] <http://www.iii.co.uk/articles/441171/cryptocurrencies-plunge-china-bans-initial-coin-offerings>

[8] <https://siliconangle.com/blog/2017/09/03/china-bans-initial-coin-offerings-pending-review>

[9] <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR117>

[10] <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR117>

[11] <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR117>

[12] <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR117>

[13] <http://www.sfc.hk/edistributionWeb/gateway/EN/news-and-announcements/news/doc?refNo=17PR117>