

Article Information

Authors: Michael Bacina, Will Fennell

Service: Blockchain

CryptoLaw: The Business of Bitcoin

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1. Introduction

Since Bitcoin was introduced in 2008, it has continued to grow in popularity, public awareness and adoption. As of the time of writing, the market capitalisation of Bitcoin is almost [USD\\$126 billion](#) with an estimated [15 million users](#). With mixed reports as to the popularity of Bitcoin as a means of payment, the leading online payment gateway, Bitpay, was on track in December 2017 to process US\$1 Billion in transactions per year.

Never before has the world seen such widespread and fast adoption of a socially agreed medium of exchange which is not backed by a government.

While Bitcoin adoption still has a long way to reach daily mainstream use, one aspect which will directly impact the speed of that adoption is the degree to which governments either help or hinder those wishing to use Bitcoin as a store of value, to trade, or in business to business or business to business transactions.

Despite sensationalist headlines bringing up Bitcoin's past association with the Darkweb, governments in Western Countries have been supportive of the innovation that Distributed Ledger Technology and Bitcoin brings to the economy.

2. Regulation of distributed ledger technology vs regulation of cryptocurrencies

This paper is limited to a summary of the key regulatory steps which have been taken by legislatures and financial services regulators in the Asia Pacific region and the United States in respect of the regulation of Bitcoin and cryptocurrencies. Many of these regulations touch upon the regulation (or potential regulation) of so-called Initial Coin Offerings (ICOs). ICOs occur when a group or corporate entity create and sell their own cryptographic token (or 'coin') as part of raising funds to build a blockchain platform or create a new currency as a means of exchange. The legislative response to distributed ledger technology itself is generally addressed together with cryptocurrencies by legislatures, in part due to the large amounts of money being raised during ICOs.

The approach of different countries to the regulation and tax treatment of Bitcoin in particular, and cryptocurrencies in general, is marked, ranging from complete bans through to pro-active regulation and encouragement of further development of this new technology.

3. Regulation of Bitcoin

Australia

In December 2014, the Australian Taxation Office (ATO) issued a number of public rulings outlining its views on the application of Australia's domestic taxation laws in respect of transactions involving Bitcoin. Broadly the ATO proffered its views that:

- [Bitcoin was a capital gains tax asset and therefore dealings in Bitcoin could result in both capital gains and losses](#)

[for taxpayers](#)

- Bitcoin held for the purpose of sale or exchange in the ordinary course of a business, is subject to the [trading stock provisions](#);
- The provision of Bitcoin by an employer to an employee comprises a “[property fringe benefit](#)” for which fringe benefits tax is payable;
- [Bitcoin is not ‘foreign currency’](#) (if it were foreign currency, gains and losses would have been on income account only);
- That where Bitcoin was used for business transactions, a [1992 ruling dealing with barter transactions applies](#); and
- A transfer of Bitcoin from one entity to another is a [supply for GST purposes](#) (which potentially led to double GST as both the party supplying goods, and a party paying for goods using Bitcoin could each be making taxable supplies on which GST was payable).

On 1 July 2017 Australia [removed the potential double-taxation of digital currency](#). However notwithstanding the advances in relation to the GST treatment of cryptocurrency, in 2017 and 2018 the ATO updated its views on GST and digital currencies. Broadly those updated views included a statement that the GST treatment of an ICO depends upon nature of the underlying token. Whilst ICOs involving traditional cryptocurrencies such as Bitcoin would not attract GST, where the token was exchangeable for goods or services, the sale of the token might be subject to GST. This appears unusual when applied to so called “utility” or “access” tokens which would be more analogous to vouchers or pre-paid services, and which would normally attract GST at [the point of use, not the point of purchase](#).

However perhaps the biggest issue presently facing ICOs in Australia is the treatment of tokens for income tax purposes as trading stock rather than as a form of security, meaning that funds raised on an ICO are potentially subject to taxation. Additionally, where ICOs receive other currencies other than fiat on an ICO, due to the volatility of cryptocurrency it is prudent for the issuers to convert those currencies to fiat on the day of the ICO. Given that many ICOs are being undertaken for the purpose of funding a related digital business, if taxation of proceeds applies to an ICO this can have a detrimental effect on the amount raised.

There are a number of Private Rulings by the ATO which are pending and, once released, should assist in providing greater certainty over how the ATO will treat certain cryptocurrency transactions.

On 4 October 2017, the Australian Securities and Investment Commission released guidance concerning ICOs, indicating that ASIC would consider each ICOs coin or token’s structure and features when forming a view as to whether any particular ICO would fall into a [regulated product category](#). As yet ASIC has invited early engagement by those seeking to operate an ICO, but has not commenced any prosecutions of ICOs. Further guidance from ASIC is expected this year concerning ICOs.

Further to this, on 3 April 2018, amendments to the *Anti-Money Laundering and Counter Terrorism Financing Act 2006* will take effect which will include Bitcoin and other cryptocurrencies under a definition of “digital currency” and which will require the registration of digital currency exchanges with the government’s anti-money laundering agency, AUSTRAC. Those digital currency exchanges will be required to comply with and maintain an Anti Money Laundering Policy to report suspicious transactions and maintain records for 7 years of trading activity.

It is interesting to note that the changes to the AML/KYC Act arose in part as a result of cryptocurrency exchanges proactively approaching regulators asking to be brought in from the cold. The explanatory memorandum to the amending bill states that the changes were needed in part to address a perception of illegitimacy caused by the regulatory gap. The memorandum further states that leaving cryptocurrency outside of the AML/CTF Act could stifle further innovation in the space.

China

Between 2014 and 2017, the Chinese market made up approximately 90 percent of global Bitcoin trading volume. Despite this, and China taking a very “hands off” approach to Bitcoin, and even indicating in 2016 they would be considering a state issued cryptocurrency, in September 2017 the Chinese government banned ICOs and on this news the [price of Bitcoin dropped sharply](#). Financial institutions and third-party payment providers are prohibited from using, accepting or selling virtual currencies, including Bitcoin.

Bitcoin mining companies are relocating from China, principally to Canada, and other cryptocurrency businesses are looking to leave to find jurisdictions which embrace such innovation. Hong Kong is viewed by many as too close to China, and the climate is ill-suited to the needs of large mining operations.

China is the largest country to have effectively banned cryptocurrencies and has the most restrictive regulations limiting the use of Bitcoin. While reason for the ban is not public (other than government statements about protecting people from speculation), the ease with which Bitcoin and other cryptocurrencies enable Chinese citizens to bypass the otherwise very

strict capital controls implemented by the Chinese government on movement of currency out of China likely play a part in the regulator's decisions.

Hong Kong

While ICOs are banned in China, they are permitted in Hong Kong if the tokens on issue are purely for access to a platform or product and do not represent ownership of an underlying asset. The regulatory position remains unclear, as the Securities and Futures Commission (SFC) issued a notice on 5 September 2017 declaring while "typical" ICOs would be considered "virtual commodities" not subject to specific regulation, certain features of a coin could cause it to be considered a share, debenture or interest in a collective investment scheme. This is not too dissimilar a position to that taken in Australia by ASIC.

Japan

Japan is considered one of the most progressive jurisdictions regulating cryptocurrency and the Financial Services Agency of Japan has worked with cryptocurrency exchanges to regulate them.

It is estimated that around 1 million Japanese own Bitcoin.

On 1 April 2017, Japan enacted a law known as the Virtual Currency Act (**VCA**) which authorised the use of digital currency as a method of payment. [The VCA defines a virtual currency as a digital token with:](#)

1. Asset-like values (limited to those items electronically recorded by electronic or other equipment and excluding Japanese currency, foreign currency, and currency-denominated assets; the same applies to the item below) usable as payment to indefinite parties for the cost of purchase or rent of items or receipt of services and which can be transferred by means of electronic data processing systems; or
2. Asset-like values that can be used in exchange with indefinite parties for those items described in the preceding item and which can be transferred by means of electronic data processing systems.

The VCA states that Bitcoin is considered both an asset and a payment method but importantly that it is not a financial instrument. The VCA does not, however, go so far as to declare Bitcoin legal tender.

In September 2017, the Financial Services Agency of Japan started granting licenses to 11 digital currency exchanges in a further move to regulate cryptocurrency trading. In recognising Bitcoin as a virtual currency and a valid means of payment, Japan's government has accelerated the acceptance of Bitcoin with [an estimated 10,000+ stores in Japan now accepting Bitcoin](#), including major brands and an airline.

Singapore

The Monetary Authority of Singapore (**MAS**) and the Singaporean government have been supportive of Bitcoin and cryptocurrencies in general as is evidenced by a large number of ICOs being run from Singapore and regulation of Bitcoin commencing in Singapore in 2014.

In Singapore, ICOs are regulated in a similar fashion to Australia and Hong Kong. If a coin's features causes it to fall within the definition of traditional financial products, such as a share, derivative or collective investment scheme, then it will need to comply with the existing regulatory regime.

In November 2016 MAS partnered with the R3 Consortium as one of the earliest government projects to discover uses for blockchain technology. Specifically, Project Ubin is seeking to find ways for financial markets to operate more efficiently.

Earlier this year, Singapore made clear that it will treat Bitcoin and cryptocurrency transactions as if they were cash transactions made in fiat for the purposes of [anti-money laundering rules and regulations](#) but leaders have also made clear they see no 'strong case' to ban Bitcoin or cryptocurrencies. They have indicated concern over [retail investors speculating in cryptocurrency markets](#) and Singapore's central bank and MAS has very recently signalled it is [considering additional rules to protect investors](#).

Singapore is working to finalise and pass the Payment Services Bill, which is expected to bring Bitcoin and cryptocurrency under a registration scheme as 'providing virtual currency services', 'dealing in virtual currency' and 'facilitating the exchange of virtual currency' [will be regulated activities if the bill passes in its current form](#).

South Korea

In 2013, the Korean Financial Supervisory Service and other agencies announced that “cyber currency” is not “real legal currency” and does not meet the standards required for currency transactions.

Despite this, South Korea has always enjoyed a strong position in global trading volumes for Bitcoin.

During 2017 regulators in South Korea started introducing further regulations, including the Financial Services Commission of Korea [issuing a complete ban in June 2017 on Bitcoin futures trading](#) with ICOs banned in the country and [mixed messages](#) on whether cryptocurrency exchanges will be permitted to operate. In early 2018, [the Blue House announced](#) there would be no ban on cryptocurrency trading in the short term.

Even with the mixed messages, local Korean media reported that trading volumes in February 2018 had reached new highs, with USD\$250M traded in Bitcoin in 24 hours on 19 February 2018 on one of the most popular cryptocurrency exchanges, and South Korea remains a highly active jurisdiction for cryptocurrency trading.

United States of America

The USA has had a mixed attitude to Bitcoin and cryptocurrencies to date, with the Securities and Exchanges Commission taking a hard line towards ICOs and the Internal Revenue Service cracking down on those trading cryptocurrencies but not declaring gains on their taxes. The IRS has provided guidance that defines “virtual currency” as property for tax purposes and [accepts that some jurisdictions treat virtual currency as “real” currency \(i.e. like legal tender\)](#).

The SEC and Commodity Futures Trading Commission have all been active in 2017 with announcements being made, in particular around ICOs. The SEC has not approved the listing of any exchange traded financial products which hold cryptocurrency and has not registered any ICOs as being authorised offers of securities.

The SEC has been active in pursuing ICOs which it believes constitutes the offer of unregistered securities and has been [supportive of action against a suspected ponzi ICO scheme in Canada](#).

Individual states have taken the lead over the Federal agencies in the US, with [Arizona](#), [Hawaii](#), [New Hampshire](#), [Illinois](#), [Vermont](#) and [Florida](#) all passing or considering laws which provides for courts to rely on information stored in a blockchain as evidence of a fact and including a statutory definition of smart contracts. [Nevada permits businesses which are required to store records in writing to use the blockchain to do so](#).

Further, the National Conference of Commissioners on Uniform State Laws voted in July 2017 to approve a model act for regulation of digital currency businesses at a state level. On 6 February 2018 the American Bar Association approved a [Uniform Regulation of Virtual-Currency Businesses Act](#) which defines “virtual currency” as a digital representation of value that is used as a medium of exchange, unit to account or a store of value and which is not legal tender. The Act further provides for a three category approach to businesses engaging in virtual currency businesses, being 1) exemption, 2) registration or 3) licensing. The uniform act includes consumer protection provisions.

This “bottom up” legislative approach may see change at the top as the SEC comes under pressure from states seeking to benefit from the popularity in cryptocurrencies.

Wyoming in particular has recently surged to the forefront of US states in passing some of [the most comprehensive laws defining various cryptographic tokens as part of an attempt to regulate ICOs](#) providing for a definition of “utility” tokens which are deemed not to be securities.

4. What's next?

Given the global nature of cryptocurrency, we hope that legislative responses to Bitcoin in particular and cryptocurrencies in general will continue to strike a fair balance encouraging innovation in this exciting new space while providing protection to potential backers of cryptocurrency projects.

With great thanks to [Will Fennell, Special Counsel](#), for his invaluable assistance in preparing this article. The author holds cryptocurrencies and is an advisor to a number of cryptocurrency projects.

This article was first published in Asian