

## Telecommunications, Media & Technology Update

### VIRTUAL CURRENCIES: THE RISE AND REGULATION OF INITIAL COIN OFFERINGS

#### A. Introduction

The popularity and widespread use of virtual currencies (also referred to sometimes as “digital currencies” or “*cryptocurrencies*”) has grown extensively.

Particularly, the viability and usage of virtual currencies has in recent times incited even more fervour amongst start-up communities as it has been employed successfully as a means raising funds for businesses. In 2017 alone, it was reported that more than \$1.5 billion was raised through more than 90 Initial Coin Offerings (or “ICOs” for short).<sup>1</sup>

The newfound surge in the usage of ICOs in Singapore has prompted the Monetary Authority of Singapore (“MAS”) to issue regulatory guidelines in August 2017, to clarify their position regarding digital coin (or token) sales via an ICO.

#### B. What are virtual currencies?

Virtual currencies generally refer to a form of payment method that exists only in electronic form and is therefore unlike normal legal tender, which is tangible. They can be transferred between entities or users across computers, smartphones and wirelessly via the internet. This thus enables the borderless transfer of ownership as well as instantaneous transactions.

Virtual currencies may therefore be considered as a medium of exchange, a unit of account or a store of value, and which are commonly used to purchase specific goods and/or services from a particular vendor who recognises and is willing to accept such currencies.

Another type of virtual currency would be cryptographically-secured coins (i.e. encrypted coins or tokens). Such coins are auto-tracked and self-regulate the generation of units, and are even able to verify the transfer of funds without the oversight of a central bank. These decentralized coins therefore

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<sup>1</sup> **CoinDesk ICO Tracker All-Time Cumulative ICO Funding**. Last updated 16 September 2017 at URL: <https://www.coindesk.com/ico-tracker/> and last accessed on 20 September 2017.

provide a means for individuals to store their wealth in a way that is not restricted by any physical or geographical boundaries, and which are not subject to traditional means of seizure or confiscation.

C. What is an ICO and what makes them especially attractive?

ICOs are predominantly used by smaller companies (usually tech *start-ups*) to raise capital. Although ICOs may sound similar to a traditional Initial Public Offering (“IPO”), there is one big difference among others. ICOs can be used to bypass the otherwise rigorously regulated capital-raising processes utilised by venture capitalists or banks.

This feature is exactly what makes ICOs so attractive because if successful it enables start-ups to raise the necessary capital and thus increase their worth in an incredibly quick timespan.

D. How do ICOs work and how are virtual currencies utilised in ICOs?

Virtual currencies are typically offered through an ICO, or some other investment scheme, to members of the public (or “Backers”) for purchase. Upon purchase, these Backers are then provided with digital coins, typically with a widely-used virtual currency (such as Bitcoin or Ether).<sup>2</sup> A white paper is also prepared, which outlines the terms of the ICO and the goal of the project. The function of these digital coins are typically used to either purchase products or services offered by the issuing company<sup>3</sup>, give the backer an entitlement to dividends, or may even be traded by speculators.

Recent clarifications issued by the MAS<sup>4</sup> has been brought about by two predominant reasons:

- Firstly, ICOs are vulnerable to money laundering and terrorist financing activities due to the anonymous nature of the transactions, and the ease with which large sums of monies may be raised in a short period of time.

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<sup>2</sup> **Consumer Advisory on Investment Scheme Involving Digital Tokens (Including Virtual Currencies)**. Published 10 August 2017 at URL: <http://www.mas.gov.sg/News-and-Publications/Media-Releases/2017/Consumer-Advisory-on-Investment-Schemes-Involving-Digital-Tokens.aspx> and last accessed on 5/9/2017.

<sup>3</sup> *Ibid.*

<sup>4</sup> **MAS clarifies regulatory position on the offer of digital tokens in Singapore**. Published 1 August 2017 at URL <http://www.mas.gov.sg/News-and-Publications/Media-Releases/2017/MAS-clarifies-regulatory-position-on-the-offer-of-digital-tokens-in-Singapore.aspx> and last accessed on 5/9/2017.

- Secondly, the range of functions performed by digital coins has recently evolved beyond merely functioning as a form of virtual currency. Digital coins may now also represent ownership or a security interest over an issuer's assets or property which may therefore constitute an offer of shares or units in a collective investment scheme under the Securities and Futures Act (Cap. 289 of Singapore) ("**SFA**"). Furthermore, digital coins may also represent a debt owed by an issuer and be considered a debenture under the SFA.

*E. What is Singapore's current regulatory stance on ICOs in accordance with MAS's recent August 2017 update? When would an ICO need to be approved?*

With the new August 2017 clarifications, the offer or issue of digital coins will now be regulated by MAS if the digital coins constitute products regulated under the SFA.

Where digital coins fall within the definition of securities in the SFA, issuers of such coins would be required to lodge and register a prospectus with the MAS prior to the offer of such coins, unless otherwise exempted. This prospectus requirement would mean that some ICOs would not differ from the conventional IPO of shares, whereby a disclosure document is required and would provide an investor with the requisite information to make an informed assessment.<sup>5</sup>

However, the difficulty will likely lie in correctly ascertaining whether a specific ICO constitutes a security or not.

If the SFA is to apply, then issuers and intermediaries of digital coins would then also be subject to the licensing regime and requirements under the SFA and also the Financial Advisers Act (Cap. 110), unless exempted. It is important to note that the, platforms (online or otherwise) facilitating the secondary trading of such coins will also have to be approved and/or recognised by the MAS as an approved exchange or market operator respectively under the SFA.<sup>6</sup>

Internationally, different countries have since reacted to ICOs somewhat differently. The U.S. position is generally similar to the one taken in Singapore, with the American Securities and Exchange Commission stating in July 2017 that federal securities law will apply over digital coin sales where the digital coins had the same qualities as securities. China on the other hand, has taken the more extreme position by declaring all ICOs illegal and announced that any money raised from Chinese investors in

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<sup>5</sup> *Ibid.*

<sup>6</sup> *Ibid.*

ICOs be refunded. South Korea has also recently announced that it too will be banning funds raising through all forms of virtual currencies.

The current regulatory regime is in a state of flux at this juncture, much like the underlying technologies and word of virtual currencies, and is constantly evolving. We expect to provide more updates on this area, as the law develops.

*Should you have any queries as to how this update may affect your organisation or require further information, please do not hesitate to email us.*



Max Ng  
Managing Director  
Gateway Law Corporation

Email: max.ng@gateway-law.com



Mitchel Chua  
Senior Associate  
Gateway Law Corporation

Email: mitchel.chua@gateway-law.com

*This article is intended to highlight the salient issues relating to the recent August 2017 MAS clarification on virtual currencies that has been published in Singapore, and it is not intended to be comprehensive nor should it be construed as legal advice. This article is updated as at 3 October 2017. The authors of this article would like to express their appreciation to Ms Melanie Leow, who interned at Gateway Law Corporation, for her assistance and contribution to this article.*

Since the time of this article, MAS has issued a further [Guide to Digital Token Offerings](#). You may wish to refer to our further [update](#) on this Guide.