



BLOCKCHAIN, CRYPTOCURRENCY & THE LEGAL ENVIRONMENT IN SINGAPORE

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I. Introduction

In the wake of the recent explosion of the use of blockchain and cryptocurrencies in Singapore, we examine and analyse below some of the key components of the ecosystems such as the importance of solutions, usefulness of cryptocurrencies, and Singapore legal and regulatory aspects, including legal documentation, “Know-Your-Customer” and Anti-Money Laundering considerations, and intellectual property.

II. The Bedrock is the “Solution”

In a typical blockchain cryptocurrency ecosystem, we are in effect creating a community whose members all have roles to play for the implementation of a solution. Also referred to as a protocol or platform, the solution is the crucial bedrock of the ecosystem. Irrespective of capital raised or number of supporters, the ecosystem is unlikely to succeed without a practical, useful and innovative solution. Not to belittle the technology, thought processes and sophistication behind some of the solutions being presented, the same simplistic market feasibility exercises of the past could in fact work in determining the predicted success or not of a solution. Token or coin generators have reportedly at times blamed other resources such as crypto traders, regulators and even lawyers for the failures of their ecosystems, when in fact the issues lay with the usefulness, practicality, value and sustainability of the solutions they had provided. So, before even starting, the critical question is “Is our solution useful, practical and desirable, and does it make business sense?”

III. Cryptocurrency

As the world crypto market gathers pace and some coins hit an all time high in value, it is useful to examine why this digital currency is being favoured over conventional or ‘fiat’ currency. It should firstly be clarified that when tokens or coins are generated and then used in an ecosystem, these coins or tokens then become a new cryptocurrency. The list of “cryptos” can therefore be infinite.

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Some of the key favourable tenets and advantages of cryptocurrencies are as follows:

(1) Decentralisation

There is this concept of a shared virtual “community” because the cryptocurrency is essentially owned and controlled by the people. Instead of a centralized government or regulatory body, the “blockchain” or public ledger is essentially a decentralised platform stored collectively on computers on a global scale and governed by mathematical algorithms and the people. Some have even compared individual ecosystems to the creation of new “miniature countries”.

(2) Unlimited usage

Cryptocurrency may be easily sent immediately to and from anyone at any time with minimal or no fees. In a typical cryptocurrency ecosystem, there is a community of users who are transacting value peer-to-peer, which means that conventional third parties or intermediaries are no longer required, thus reducing costs to the users.

(3) Transparency

All technical specifications and whitepapers are published online for the public to access and there is no single point of control or failure.

(4) Supply control

The offeror or generator of the cryptocurrency may predetermine and control the supply of a cryptocurrency and the currency works because of its controlled and limited supply. Governments have no influence in this domain.

(5) Privacy

There is a certain amount of anonymity attached to consumer's identities insofar as cryptocurrency transactions are concerned.

(6) Reduced Costs

With the use of smart contracts, obligations are automatically enforced in a transparent and a conflict-free way which also cuts down on costs.

IV. Why is Singapore an attractive option ?

Singapore has been described by many experts as a conducive landscape for cryptocurrencies and blockchain technology to flourish due to its superb communications network, its global reputation as a financial hub, non interference by regulators, and growing interest in FinTech.

Unlike some other countries, Singapore has taken a liberal approach and opted for a more balanced view – it has embraced crypto start-ups and the government has set into motion large scale initiatives to drive FinTech growth and innovation. The challenge faced by the regulator, which is the Monetary Authority of Singapore (“MAS”), is in ensuring the lay

investor and the public are adequately protected from scam offerings and to instill proper safeguards, but at the same time, not to over-regulate so as to stifle the crypto environment.

Interest in the cryptocurrency space in Singapore is from investors and corporates (both local and foreign) alike. The individual investors or token purchasers want to invest in the various cryptocurrencies being issued, while corporates are keen on conducting a token generation event related to the issue of digital tokens in Singapore (“**TGE**”) and raising capital. (Please note that we will loosely use both the terms Initial Coin Offering or “ICO and “TGE” interchangeably).

Singapore is viewed as an attractive jurisdiction to conduct a TGE because, among other things; (1) it is easy to incorporate an entity in Singapore; and (2) the **MAS** has taken the position (as of 1st August 2017) that it will not regulate the offer or issue of digital tokens provided the digital tokens do not constitute products that are regulated under the Securities and Futures Act (Cap. 289) (“**SFA**”) in Singapore. The lack of express prohibition on the issuance of digital tokens and the perception that decentralised cryptocurrencies are considered unregulated assets is therefore the reason Singapore, along with Switzerland, has been identified by many as a ‘crypto-haven’.

Having said that, it must be noted that more recently, after the publication of “The DAO Report” in July 2017 by the U.S. Securities and Exchange Commission, MAS issued ‘A Guide to Digital Token Offerings’ on 15 November 2017. The Guide elaborated that the offering of digital tokens must comply with the SFA only if the digital token constitutes a product regulated under the SFA.

In its guide, MAS also provides several hypothetical case studies of digital tokens which would be regulated in Singapore and others which would fall outside the ambit of its regulatory framework. There is now a clearer picture for potential TGE’s or ICO’s on which of their offerings may be caught by MAS’ regulatory framework.

MAS has also said that it will carefully assess the nature, composition and specifications of the digital token in its assessment, and has created a “Sandbox” approach in doing so and in an effort to provide speedy replies.

This brings us to the second step in the regulatory analysis: The MAS guidelines above refer to the characterization of the token itself. It could very well be that the token itself is not regulated, but that the solution or activity of the platform is regulated. For example, if tokens are used for a protocol whose activity is regulated in Singapore, such as insurance or moneylending, then the licenses required by these activities would need to be procured. So there could be a situation where the ICO does not fall within the ambit of regulation, but that the solution in the operating entity is regulated by Singapore law.

Notwithstanding regulation and facility of processes, an investor or supporter must take into account that there will always be inherent commercial risks in the investment, largely due to the success of the solution as discussed above, that could result in someone losing all or a substantial portion of its investment.

V. Typical legal documentation used for TGE/ICO

The practical reality then is that the only recourse available to a supporter or investor investing or buying into an unregulated digital token or coin offering may be the legal provisions found in the commercial agreements entered into between an investor or supporter and the Token/Coin Generator.

In terms of structuring a TGE or ICO, one way might be for the actual Generator to be set up as a foundation, which is usually in the form of a company limited by a guarantee, as this company is meant to carry out non-profit making activities that have some basis of national or public interest. The actual platform may be operated by a separate operating company. This can be a private limited company which should ideally be responsible for the on-boarding of the users and platform development and operation. The agreements typically involved in such a structure are both a development and service contract.

We set out below some of the other documentation and agreements typically used in digital token or coin offerings in Singapore:

(1) White Paper

The 'White Paper' is a document that provides an investor with a preliminary understanding of the intent of the Token or Coin Generator, objectives of the offering, technology behind the project (for example if it is underpinned by block-chain technology), type of corporate structure used in a potential offering and also the financial modelling of the token generation.

The White Paper is often the first document published on the website of the Token Generator and serves as an 'expression of interest' to the potential investor. It is imperative for a potential investor or supporter to review the information in the White Paper carefully and ask the right questions so that he or she understands the technology behind the digital tokens issuance for example, prior to making an investment.

The White Paper should ideally contain the commercial, technological and financial information and details of the offering in jargon and language which can be understood by laypersons. The draft White Paper is usually also the first item requested when the Generator speaks with potential investors, advisers or lawyers.

(2) Pre-Sale Agreement

The Pre-Sale Agreement ("**PSA**"), as its name implies, is an agreement that is entered into between selected investors and the Generator ahead of the 'crowd-sale'.

The pre-sale is usually convened prior to the main TGE or ICO process in order for the Generator to pre-sell the digital tokens or coins to a select group of potential supporters or investors (such as family, friends and selected investors) at discounted prices and for a limited period of time as determined by the Generator. The pre-sale is also a useful way for the Generator to gauge interests in the digital token offering

ahead of the crowd-sale with the TGE/ICO. It must also be emphasized that selling too much at a pre-sale may not in fact be a good thing because for an ecosystem or a community to be successful, it in many cases, needs a large number of supporters. Selling fast to a small group may limit the number and scope of supporters, and ultimately the success of a community.

In certain transactions, parties may decide to enter into an escrow arrangement ahead of the TGE whereby an escrow agent will hold relevant cryptocurrency in trust for the investor, which will be released to the Token Generator upon certain trigger events occurring.

(3) TGE Terms & Conditions

The TGE or ICO Terms & Conditions (the “**TGE Documentation**”) is the main documentation used in the ‘crowd-sale’.

The TGE Documentation usually contains, among other things, information about the Token Generator, restrictions on distribution of the tokens, disclaimer, indemnification and self-regulation, features of the tokens, procedures for acquiring and receiving tokens and representations and warranties by investors.

In other words, the TGE Documentation is the main legally binding agreement between the investor and Token Generator and will clearly set out the liability of the Token Generator to the investor in the event that any risks in the issuance materialize. It is therefore essential for the investor to carefully review the TGE Documentation and understand its implications ahead of the investment.

The TGE Documentation will also contain certain commercial terms which will be specific to each offering and differ, depending on the factual matrix and technological details of the offering.

(4) Compliance Manual

The Token Generator would generally have in place a robust compliance manual that will contain information on general compliance of the operating entity (that issues the tokens), relationship with regulators (if applicable), corruption and anti-bribery provisions, record keeping and personal data protection policy and more importantly, anti-money laundering and fraud provisions.

MAS has emphasized that the relevant MAS Notices on Prevention of Money Laundering and Countering the Financing of Terrorism may still apply to digital tokens that fall outside the MAS regulatory framework (especially the obligations to report suspicious transactions with the Suspicious Transaction Reporting Office of the Commercial Affairs Department and prohibitions against dealing with or providing financial services to designated individuals and corporates pursuant to the Terrorism (Suppression of Financing) Act (Cap. 325)), as well as any related subsidiary legislation.

It would be prudent for an investor to ask the Token Generator if it has in place a robust compliance manual containing all of the provisions mentioned above and whether the Token Generator is willing to share such compliance manual with the investor at the opportune time.

The MAS has also announced that it will in due course establish a new payment services framework to include rules to address money laundering and terrorism financing risks related to the dealing or exchange of virtual currencies for fiat or other virtual currencies. It is advisable that the investors seek clarification from the Token Generator intermediaries on whether MAS has issued those guidelines already and if so, whether, they have put in place the required framework before investing.

VI. KYC/AML

The KYC and AML considerations as stated above and as included in the compliance manuals would also be included in the questionnaires for information on supporters or buyers of tokens. While it is unclear whether the Corruption, Drug Trafficking and other Serious Crimes (Confiscation of Benefits) Act (Cap.65A) (“CDSA”) may apply to cryptocurrencies, it would be prudent for the Generator to have in place comprehensive questionnaires collecting the identifying information under the CDSA from potential investors, or supporters either at the pre-TGE or TGE stage.

VII. Intellectual Property

In Singapore, copyright is not registrable. Therefore, in order to protect the copyright of the software source codes, the Generator should keep concise records, including dates of creation, of the software source codes for the blockchain protocol.

The Generator should also look into the possibility of registering its patent (if any) for any new processes for its blockchain technology and consider registering any trademarks it has with the Intellectual Property Office of Singapore.

VIII. Conclusion

The decentralised monetary system of cryptocurrencies is likely to be the future of financial transactions in Singapore and will also revolutionise the global financial landscape. It will be interesting to see how MAS attempts to strike a balance between permitting this virtual currency platform to grow and prosper in Singapore and enhancing an already complex regulatory regime with safeguards, with its attempts to protect not only investors, but the public at large. It will also be interesting to see what methods Token or Coin Generators take to ensure their “Solutions” make good commercial sense so that their communities or ecosystems succeed.

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