

THE VIRTUAL
CURRENCY
REGULATION
REVIEW

Editors

Michael S Sackheim and Nathan A Howell

THE LAWREVIEWS

THE VIRTUAL
CURRENCY
REGULATION
REVIEW

Reproduced with permission from Law Business Research Ltd
This article was first published in November 2018
For further information please contact Nick.Barette@thelawreviews.co.uk

Editors

Michael S Sackheim and Nathan A Howell

THE LAWREVIEWS

PUBLISHER

Tom Barnes

SENIOR BUSINESS DEVELOPMENT MANAGER

Nick Barette

BUSINESS DEVELOPMENT MANAGERS

Thomas Lee, Joel Woods

SENIOR ACCOUNT MANAGERS

Pere Aspinall, Jack Bagnall

ACCOUNT MANAGERS

Sophie Emberson, Katie Hodgetts

PRODUCT MARKETING EXECUTIVE

Rebecca Mogridge

RESEARCH LEAD

Kieran Hansen

EDITORIAL COORDINATOR

Gavin Jordan

HEAD OF PRODUCTION

Adam Myers

PRODUCTION EDITOR

Anne Borthwick

SUBEDITOR

Janina Godowska

CHIEF EXECUTIVE OFFICER

Paul Howarth

Published in the United Kingdom
by Law Business Research Ltd, London
87 Lancaster Road, London, W11 1QQ, UK
© 2018 Law Business Research Ltd
www.TheLawReviews.co.uk

No photocopying: copyright licences do not apply.

The information provided in this publication is general and may not apply in a specific situation, nor does it necessarily represent the views of authors' firms or their clients. Legal advice should always be sought before taking any legal action based on the information provided. The publishers accept no responsibility for any acts or omissions contained herein. Although the information provided is accurate as of October 2018, be advised that this is a developing area.

Enquiries concerning reproduction should be sent to Law Business Research, at the address above.

Enquiries concerning editorial content should be directed
to the Publisher – tom.barnes@lbresearch.com

ISBN 978-1-912228-77-5

Printed in Great Britain by
Encompass Print Solutions, Derbyshire
Tel: 0844 2480 112

ACKNOWLEDGEMENTS

The publisher acknowledges and thanks the following for their learned assistance throughout the preparation of this book:

ALLEN & GLEDHILL LLP

AMERELLER

ANDERSON MORI & TOMOTSUNE

ARTHUR COX

BECH-BRUUN

BRANDL & TALOS RECHTSANWÄLTE GMBH

CLIFFORD CHANCE LLP

DENTONS

GERNANDT & DANIELSSON ADVOKATBYRÅ

GTG ADVOCATES

HARNEYS

HENGELER MUELLER PARTNERSCHAFT VON RECHTSANWÄLTEN MBB

JONES DAY

KIM & CHANG

LINKLATERS

MARVAL, O'FARRELL & MAIRAL

NISHITH DESAI ASSOCIATES

PINHEIRO NETO ADVOGADOS

RUSSELL MCVEAGH

SCHELLENBERG WITTMER LTD

SCHILTZ & SCHILTZ SA

SCHJØDT

SIDLEY AUSTIN LLP

STIBBE

STIKEMAN ELLIOTT LLP

TFH RUSSIA LLC

URÍA MENÉNDEZ

WEBB HENDERSON

YIGAL ARNON & CO

CONTENTS

PREFACE.....	vii
<i>Michael S Sackheim and Nathan A Howell</i>	
Chapter 1	ARGENTINA..... 1
<i>Juan M Diebl Moreno</i>	
Chapter 2	AUSTRALIA..... 6
<i>Ara Margossian, Marcus Bagnall, Ritam Mitra and Irene Halforty</i>	
Chapter 3	AUSTRIA..... 18
<i>Nicholas Aquilina and Martin Pichler</i>	
Chapter 4	AZERBAIJAN 32
<i>Ulvia Zeynalova-Bockin</i>	
Chapter 5	BELGIUM 39
<i>Michiel Van Roey and Louis Bidaine</i>	
Chapter 6	BRAZIL..... 60
<i>Fernando Mirandez Del Nero Gomes, Tiago Moreira Vieira Rocha and Alessandra Carolina Rossi Martins</i>	
Chapter 7	CANADA..... 72
<i>Alix d'Anglejan-Chatillon, Ramandeep K Grewal, Éric Lévesque and Christian Vieira</i>	
Chapter 8	CAYMAN ISLANDS 84
<i>Ian Gobin and Daniella Skotnicki</i>	
Chapter 9	CHINA..... 96
<i>Annabella Fu</i>	
Chapter 10	DENMARK..... 108
<i>David Moalem and Kristoffer Probst Larsen</i>	

Contents

Chapter 11	GERMANY.....	118
	<i>Matthias Berberich and Tobias Wohlfarth</i>	
Chapter 12	HONG KONG	137
	<i>Graham Lim and Sharon Yiu</i>	
Chapter 13	INDIA	144
	<i>Vaibhav Parikh, Jaideep Reddy and Arvind Ravindranath</i>	
Chapter 14	IRELAND	157
	<i>Maura McLaughlin, Pearse Ryan and Caroline Devlin</i>	
Chapter 15	ISRAEL.....	162
	<i>Adrian Daniels, Roy Keidar, Dafna Raz, Eran Lempert and Yuval Shalheveth</i>	
Chapter 16	JAPAN	174
	<i>Ken Kawai and Takeshi Nagase</i>	
Chapter 17	KOREA	184
	<i>Jung Min Lee, Joon Young Kim and Samuel Yim</i>	
Chapter 18	LUXEMBOURG.....	194
	<i>Jean-Louis Schiltz and Nadia Manzari</i>	
Chapter 19	MALTA.....	204
	<i>Ian Gauci, Cherise Abela Grech, Bernice Saliba and Samuel Gandin</i>	
Chapter 20	NEW ZEALAND.....	213
	<i>Deemle Budhia and Tom Hunt</i>	
Chapter 21	NORWAY.....	224
	<i>Klaus Henrik Wiese-Hansen and Vegard André Fiskerstrand</i>	
Chapter 22	PORTUGAL.....	233
	<i>Hélder Frias and Luís Alves Dias</i>	
Chapter 23	RUSSIA	243
	<i>Maxim Pervunin and Tatiana Sangadzhieva</i>	
Chapter 24	SINGAPORE.....	257
	<i>Adrian Ang, Alexander Yap, Anil Sberghill and Samuel Kwek</i>	

Contents

Chapter 25	SPAIN.....	266
	<i>Pilar Lluesma Rodrigo and Alberto Gil Soriano</i>	
Chapter 26	SWEDEN.....	274
	<i>Niclas Rockborn</i>	
Chapter 27	SWITZERLAND.....	283
	<i>Olivier Favre, Tarek Houdrouge and Fabio Elsener</i>	
Chapter 28	UNITED ARAB EMIRATES.....	297
	<i>Silke Noa Elrifai and Christopher Gunson</i>	
Chapter 29	UNITED KINGDOM.....	310
	<i>Peter Chapman and Laura Douglas</i>	
Chapter 30	UNITED STATES.....	330
	<i>Sidley Austin LLP</i>	
Appendix 1	ABOUT THE AUTHORS.....	381
Appendix 2	CONTRIBUTING LAW FIRMS' CONTACT DETAILS.....	407

PREFACE

On 31 October 2008, Satoshi Nakamoto published a white paper describing what he referred to as a system for peer-to-peer payments, using a public decentralised ledger known as a blockchain and cryptography as a source of trust to verify transactions. That paper, released in the dark days of a growing global financial market crisis, laid the foundations for Bitcoin, which would become operational in early 2009. Satoshi has never been identified, but his white paper represented a watershed moment in the evolution of virtual currency. Bitcoin was an obscure asset in 2009, but it is far from obscure today, and there are now many other virtual currencies and related assets. In 2013, a new type of blockchain that came to be known as Ethereum was proposed. Ethereum's native virtual currency, Ether, went live in 2015 and opened up a new phase in the evolution of virtual currency. Ethereum provided a broader platform, or protocol, for the development of all sorts of other virtual currencies and related assets.

Whether Bitcoin, Ether or any other virtual currency will one day be widely and consistently in use remains uncertain. However, the virtual currency revolution has now come far enough and has endured a sufficient number of potentially fatal events that we are confident virtual currency in some form is here to stay. Virtual currencies and the blockchain and other distributed ledger technology on which they are based are real, and are being deployed right now in many markets and for many purposes. The technology has matured beyond hypothetical use cases and beta testing. These technologies are being put in place in the real world, and we as lawyers must now endeavour to understand what that means for our clients.

Virtual currencies are essentially borderless: they exist on global and interconnected computer systems. They are generally decentralised, meaning that the records relating to a virtual currency and transactions therein may be maintained in a number of separate jurisdictions simultaneously. The borderless nature of this technology was the core inspiration for *The Virtual Currency Regulation Review (Review)*. As practitioners, we cannot afford to focus solely on our own regulatory silos. For example, a US banking lawyer advising clients on matters related to virtual currency must not only have a working understanding of US securities and commodities regulation; he or she must also have a broad view of the regulatory treatment of virtual currency in other major commercial jurisdictions.

Global regulators have taken a range of approaches to responding to virtual currencies. Some regulators have attempted to stamp out the use of virtual currencies out of a fear that virtual currencies such as Bitcoin allow capital to flow freely and without the usual checks that are designed to prevent money laundering and the illicit use of funds. Others have attempted to write specific laws and regulations tailored to virtual currencies. Still others – the United States included – have attempted to apply legacy regulatory structures to virtual

currencies. Those regulatory structures attempt what is essentially ‘regulation by analogy’. For example, a virtual currency may be regulated in the same manner as money, or in the same manner as a security or commodity. The editors make one general observation at the outset: there is no consistency across jurisdictions in their approach to regulating virtual currencies. That is, there is currently no widely accepted global regulatory standard. That is what makes a publication such as *The Review* both so interesting and so challenging to assemble.

The lack of global standards has led to a great deal of regulatory arbitrage, as virtual currency innovators shop for jurisdictions with optimally calibrated regulatory structures that provide an acceptable amount of legal certainty. While some market participants are interested in finding the jurisdiction with the lightest touch (or no touch), most of our clients are not attempting to flee from regulation entirely. They appreciate that regulation is necessary to allow virtual currencies to achieve their potential, but they do need regulatory systems with an appropriate balance and a high degree of clarity. The technology underlying virtual currencies is complex enough without adding layers of regulatory complexity into the mix.

It is perhaps ironic that the sources of strength of virtual currencies – decentralisation and the lack of trusted intermediaries necessary to create a shared truth – are the same characteristics that the regulators themselves seem to be displaying. There is no central authority over virtual currencies, either within and across jurisdictions, and each regulator takes an approach that seems appropriate to that regulator based on its own narrow view of the markets and legacy regulations. We believe optimal regulatory structures will emerge and converge over time. Ultimately, the borderless nature of these markets allows market participants to ‘vote with their feet’, and they will gravitate toward jurisdictions that achieve the right regulatory balance. It is much easier to do this in a virtual business than it would be in a brick and mortar business. Computer servers are relatively easy to relocate. Factories and workers are less so.

The Review is intended to provide a practical, business-focused analysis of recent legal and regulatory changes and developments, and of their effects, and to look forward at expected trends in the area of virtual currencies on a country-by-country basis. It is not intended to be an exhaustive guide to the regulation of virtual currencies globally or in any of the included jurisdictions. Instead, for each jurisdiction, the authors have endeavoured to provide a sufficient overview for the reader to understand the current legal and regulatory environment.

Virtual currency is the broad term that is used in *The Review* to refer to Bitcoin, Ether, tethers and other stable coins, cryptocurrencies, altcoins, ERC20 tokens, digital, virtual and crypto assets, and other digital and virtual tokens and coins, including coins issued in initial coin offerings. The term is intended to provide rough justice to a complex and evolving area of law, and we recognise that in many instances the term virtual currency will not be appropriate. Other related terms, such as cryptocurrencies, digital currencies, digital assets, crypto assets and similar terms, are used throughout as needed. In the law, the words we use matter a great deal, so where necessary the authors of each chapter provide clarity around the terminology used in their jurisdiction, and the legal meaning given to that terminology.

We hope that you find *The Review* useful in your own practices and businesses, and we welcome your questions and feedback. We are still very much in the early days of the virtual currency revolution. No one can truthfully claim to know what the future holds for virtual currencies, but as it does not appear to be a passing fad, we have endeavoured to provide as

much useful information as practicable in *The Review* concerning the regulation of virtual currencies.

The editors would like to extend special thanks to Ivet Bell (New York) and Dan Applebaum (Chicago), both Sidley Austin LLP associates, without whom *The Review*, and particularly the US chapter, would not have come together.

Michael S Sackheim and Nathan A Howell

Sidley Austin LLP

New York and Chicago

October 2018

AZERBAIJAN

*Ulvia Zeynalova-Bockin*¹

I INTRODUCTION TO THE LEGAL AND REGULATORY FRAMEWORK

The rise of virtual currencies and the underlying technology in recent years have presented regulators around the world with an interesting challenge: striking a delicate balance between regulating this nascent phenomenon of decentralised currency, while avoiding overzealous regulation so as to not to stifle innovation. Azerbaijani regulators are no exception.

However, despite real concerns about fraud, money laundering and other illicit activities potentially involving the use of virtual currencies, to date there is no specific regulation of virtual currencies in Azerbaijan. There are, of course, regulations in place that would potentially be applicable to virtual currencies. However, the real challenge seems to be how to classify virtual currencies, as they possess the characteristics of various types of assets (e.g., a unit of account, a commodity or a security), thus eluding traditional regulatory definitions.

For this reason, any discussion on how virtual currencies ultimately will be regulated in Azerbaijan inevitably becomes an exercise in educated conjecture, taking into account the current understanding on the classification of virtual currencies and regulatory parameters. Depending on how virtual currencies are ultimately classified by the Azerbaijani regulators (as a unit of account, a commodity or a security), different regulations may potentially be applicable, as outlined below.

II BANKING AND MONEY TRANSMISSION

Generally, the Banking Law attributes the activity of monetary transmission (money transfer services or payment instruments) to be a licensable banking activity.² Further, the Law on Currency Regulation regards foreign currency exchange activities (i.e., engaging in the business of buying or selling foreign currencies) as an additional licensable activity in Azerbaijan in which only local banks, branches of foreign banks or certain licensed post offices may engage.³

1 Ulvia Zeynalova-Bockin is counsel at Dentons. The author would like to acknowledge the invaluable editorial guidance of James E Hogan, managing partner at Dentons.

2 Law of the Republic of Azerbaijan 'On Banks', No. 590-IIQ, dated 16 January 2004, Republic of Azerbaijan Collection of Legislation 2004, No. 03, Item 130 (in Azerbaijani), Article 32. Available at <http://e-qanun.gov.az/framework/5825>.

3 Law of the Republic of Azerbaijan 'On Currency Regulations', No. 910, dated 21 October 1994, Supreme Council of the Republic of Azerbaijan Information [Bulletin] 1995, No. 07, Item 116 (in Azerbaijani), Article 3. Available at <http://e-qanun.gov.az/framework/9238>.

The Law on Currency Regulation defines foreign currencies as moneys in the form of banknotes, treasury notes and coins in circulation that are legal tender on the territory of a foreign state or group of states. Although unlikely, it is possible that virtual currencies will be classified as a foreign currency, especially if they are recognised as legal tender in a foreign country.⁴

Therefore, entities wishing to engage in the above-mentioned activities involving a virtual currency within Azerbaijan or, potentially, Azerbaijani residents, are likely to be prevented from doing so, unless the relevant licence has been obtained.

III ANTI-MONEY LAUNDERING

When it comes to money laundering and terrorism financing, Azerbaijani law does not seem to make any material distinction between transactions carried out using a fiat currency or a virtual currency (although the latter is not specifically mentioned). For instance, any transactions involving funds received from or transferred to anonymous accounts located outside Azerbaijan or transactions where the parties cannot be accurately identified, or in cases where the submission of identification information about a customer or beneficiary is denied, as well as where identification information about a customer or beneficiary is discovered to be false, are required to be reported to the Financial Monitoring Service.⁵

The current anti-money laundering regime in Azerbaijan covers, among other regulated entities, monitoring subjects, the definition of which includes financial institutions, institutions engaged in money transmission services, investment companies, investment funds and investment fund managers.⁶ It is these monitoring subjects that have the obligation to report the foregoing transactions.

Given the potential for abuse of the anonymity present in transactions using virtual currencies and the possible implications for the enforcement of anti-money laundering legislation, this is an area where specific regulations are very likely to be enacted.

IV TAX

Given the broad definition of income under the Azerbaijani Tax Code, revenues generated by residents from trading virtual currencies are likely to be subject to taxation in Azerbaijan. Since no special regime for the taxation of capital gains exists in Azerbaijan, such revenues are likely to be subject to the progressive personal income tax (in relation to individuals not registered as entrepreneurs), a simplified tax (applicable to certain individual entrepreneurs

4 Id., Article 1.7-1, 1.7-2, and 3.

5 Law of the Republic of Azerbaijan 'On the Prevention of the Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism', No. 767-IIIQ, dated 10 February 2009, Republic of Azerbaijan Collection of Legislation 2009, No. 02, Item 58 (in Azerbaijani) [Law on the Prevention of the Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism], Article 7. Available at <http://e-qanun.gov.az/framework/16347>.

6 Id., Article 4.

and small enterprises) or corporate profit tax (applicable to enterprises with revenues exceeding a certain threshold). General taxation principles would apply to transactions using a virtual currency.⁷

It is not clear what the tax authorities' approach to enforcement would be given that, currently, the assessment of taxes on income received from abroad is largely dependent on self-declaration. However, there is a general, and rather vague, provision in the Law on Currency Regulation requiring residents of Azerbaijan to repatriate earned foreign currency reserves received from foreign economic activities, which are likely to include funds received from virtual currency trading once they are converted into fiat currency.⁸

Failure to comply with the repatriation rules may result in significant administrative fines (of up to 50 per cent of such foreign currency reserves)⁹ or, potentially, criminal liability for the management officials of the company where the funds exceed the equivalent of 20,000 Azerbaijani manats.¹⁰

V OTHER ISSUES

The 1995 Azerbaijan Constitution, which was adopted in a nationwide referendum, proclaims the Azerbaijani manat as the official currency of Azerbaijan and the only monetary unit that is recognised as legal tender within the territory of Azerbaijan.¹¹ The Constitution recognises the exclusive authority of the Central Bank of Azerbaijan to issue banknotes and mint coins.¹²

The Civil Code of the Republic of Azerbaijan, the cornerstone of commercial law in the country, goes even further by requiring that contractual monetary obligations between residents be denominated in Azerbaijani manats.¹³ Finally, wages in Azerbaijan also may only be paid in Azerbaijani manats.¹⁴

As such, virtual currencies are not, and are very unlikely to become, legal tender in Azerbaijan. In fact, recognising them as such would likely require amendments to the 1995

7 Tax Code of the Republic of Azerbaijan, approved by Law of the Republic of Azerbaijan No. 905-IQ, dated 11 July 2000, Republic of Azerbaijan Collection of Legislation 2000, No. 08, Item 583 (in Azerbaijani). Available at <http://e-qanun.gov.az/code/12>.

8 Law on Currency Regulation, Article 7.2.

9 Code of Administrative Offenses of the Republic of Azerbaijan, approved by Law of the Republic of Azerbaijan No. 96-VQ, dated 29 December 2015, Republic of Azerbaijan Collection of Legislation 2016, No. 02, Item 202 (in Azerbaijani), Article 483. Available at <http://e-qanun.gov.az/code/24>.

10 Criminal Code of the Republic of Azerbaijan, approved by Law of the Republic of Azerbaijan No. 787-IQ, dated 20 December 1999, Republic of Azerbaijan Collection of Legislation 2000, No. 04, Item 251 (in Azerbaijani), Article 208. Available at <http://e-qanun.gov.az/code/11>.

11 Constitution of the Republic of Azerbaijan, adopted at a nationwide referendum on 12 November 1995, Republic of Azerbaijan Collection of Legislation 1997, No. 03, Item 159 (in Azerbaijani), Article 19.I and 19.III. Available at <http://e-qanun.gov.az/framework/897>.

12 *Id.*, Article 19.II.

13 Civil Code of the Republic of Azerbaijan, approved by Law of the Republic of Azerbaijan No. 779-IQ, dated 28 December 1999, Republic of Azerbaijan Collection of Legislation 2000, No. 04, Item 250 (in Azerbaijani), Article 439.1. Available at <http://e-qanun.gov.az/code/8>.

14 Labour Code of the Republic of Azerbaijan, approved by Law of the Republic of Azerbaijan No. 618-IQ, dated 1 February 1999, Republic of Azerbaijan Collection of Legislation 1999, No. 04, Item 213 (in Azerbaijani), Article 174.4. Available at <http://e-qanun.gov.az/code/7>.

Constitution to be adopted in a nationwide referendum. It is not clear that the authority of the Central Bank of Azerbaijan to issue banknotes and mint coins would include minting electronic coins for a cryptocurrency protocol backed by the Central Bank.

So far, the Central Bank has not expressed any intention to engage in the minting of electronic coins, and has described its position regarding the virtual currency as conservative. In remarks made during discussions of the 2018 State Budget in the Azerbaijani Parliament, the Chair of the Central Bank, Mr Elman Rustamov, described cryptocurrencies as an instrument for investing rather than an alternative means of payment.¹⁵

VI LOOKING AHEAD

In January 2018, it was reported that a working group has been established in Azerbaijan to develop a draft law on the regulation of trade in virtual currencies.¹⁶ However, no progress seems to have been made to date. In all likelihood, and based on various public statements of local officials, Azerbaijani regulators are likely to continue to monitor¹⁷ the virtual currency space and assess regulatory measures adopted by other countries before any specific regulation is adopted.

Historically, the experience of those countries that share a common legal heritage with Azerbaijan, such as other (larger) CIS countries, is most closely studied. It so happens that the Ministry of Finance of the Russian Federation, after (reportedly) much discussion with the Russian Central Bank, recently released to the public a Draft Federal Law on Digital Financial Assets that attempts to regulate virtual currencies in Russia.¹⁸

Below we summarise the main tenets of the Draft Law, as it offers, in our view, a preview of possible avenues for the regulation of virtual currency in Azerbaijan.

i Scope of the law

Owing to the unique nature of virtual currencies, Russia has quite wisely opted to craft a separate law on the subject of virtual currencies, rather than adopt amendments to existing pieces of legislation, with blanket references to those other pieces of legislation, where necessary. The Draft Law provides a broad legal framework, while granting the right to promulgate more detailed secondary regulations to the Russian Central Bank.

-
- 15 Anvar Mammadov, 'CBA head comments on use cryptocurrency in Azerbaijan', Trend News Agency (21 November 2017), accessed on 8 August 2018, <https://en.trend.az/business/economy/2824191.html> (in Azerbaijani).
 - 16 Lada Evgrashina, 'Azerbaijan takes up crypto-currencies: the bill is being prepared, the country will be visited by co-founder Ethereum', 1news.az (29 January 2018), accessed on 6 August 2018, <http://www.1news.az/news/azerbaydzhan-vzyalsya-za-kriptovalyuty-gotovitsya-zakonoproekt-stranu-posetit-so-osnovatel-ethereum> (in Russian).
 - 17 Samuel Haig, 'Azerbaijan rejected Crypto as means of Payment', Cryptofame (4 December 2017), accessed on 18 August 2018, <https://news.bitcoin.com/azerbaijan-rejects-crypto-as-means-of-payment/>.
 - 18 Draft Federal Law of the Russian Federation 'on Digital Financial Assets', MinFin.ru (25 January 2018), accessed on 6 August 2018, https://www.minfin.ru/ru/document/?group_type=&q_4=0+цифровых+финансовых+активах&DOCUMENT_NUMER_4=&M_DATE_from_4=&M_DATE_to_4=&P_DATE_from_4=&P_DATE_to_4=&t_4=565527874&order_4=P_DATE&dir_4=DESC (in Russian).

The Draft Law purports to regulate relations arising out of the creation, issuance, storage and circulation of digital financial assets, as well as the exercise of rights and the performance of obligations under smart contracts.¹⁹

The Draft Law is expected to give a 90-day grace period, starting from the date of its official publication, before it will become effective.²⁰

Usefully, and for the first time, the Draft Law provides detailed definitions for cryptocurrency-related terms, including for cryptocurrency, tokens, smart contracts, crypto exchanges and mining, and attempts to classify them. As mentioned before, providing detailed definitions is crucial in classifying virtual currencies and embedding the regulation thereof into the larger regulatory framework.

ii Trading digital financial assets and mining

Digital financial assets are defined in the Draft Law as property in electronic form, created using cryptographic means, including cryptocurrencies and tokens. The ownership of this property is evidenced by digital entries (records) in the register of digital transactions. The Draft Law further clarifies that digital financial assets are not a legal means of payment in the territory of the Russian Federation,²¹ which makes this approach to the regulation of virtual currencies rather compelling for Azerbaijan, given the similar restriction in the 1995 Constitution of the Republic of Azerbaijan.

The Draft Law expressly recognises the right of holders of digital financial assets to trade their digital financial assets for other digital financial assets, for fiat currency (Russian roubles or foreign currency) or for other property, through the intermediation of the operators of digital financial assets exchanges.²²

Finally, the Draft Law, once adopted, will expressly legalise mining activities as entrepreneurial activities aimed at creating cryptocurrency, validation activities for the purposes of receiving compensation in the form of a cryptocurrency, or both.²³

iii Exchanges and wallets

Operators of digital financial assets exchanges are defined under the Draft Law as legal entities established in Russian law that carry out transactions for the exchange of one type of digital financial asset for another, as well as the exchange of financial assets for fiat currency. The business of operators of digital financial assets exchanges may be carried out by professional participants in the securities markets or legal entities that are organisers of trade.²⁴

Further, under the Draft Law, an electronic wallet – defined as a software and hardware tool that allows the storage of information about digital records and provides access thereto

19 Id., Paragraph 13, Article 2. Smart contracts are defined as contracts concluded in an electronic form, under which the performance of rights and obligations are carried out by the automatic transfer of digital transactions in the distributed register of digital transactions in accordance with a strictly defined sequence and upon the occurrence of certain circumstances. Rights of counterparties to smart contracts are protected in the same manner as the rights of those to contracts, concluded in an electronic form.

20 Id., Articles 1 and 5.

21 Id., Paragraph 1, Article 2.

22 Id. Paragraph 8, Article 2.

23 Id., Paragraph 10, Article 2.

24 Id., Paragraph 8, Article 2.

– may be opened by the operator of a digital financial assets exchange only after the relevant identification procedures for the wallet owner have been duly completed in accordance with the applicable Russian anti-money laundering legislation.²⁵

Again, this approach to the regulation of virtual currency would fit rather neatly into the existing Azerbaijani legal framework. This is because there are similarly regulated entities in Azerbaijan operating under the Securities Market Law²⁶ (such as, for instance, investment companies), the concept of electronic money wallets has already been introduced in relatively recent amendments to the Electronic Trading Law,²⁷ and, finally, relevant identification procedures are already in place under the Law on the Prevention of the Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism.²⁸

iv Initial coin offerings

A large part of the Draft Law addresses initial coin offerings (ICOs); namely, setting forth issuing procedures, rules for the advertisement and sale (placement) of tokens, as well as documentary, informational and disclosure requirements related to an ICO.²⁹

For each ICO, the Draft Law requires that the issuer publish, simultaneously, a public offer, an investment memorandum, rules for maintaining the register of digital transactions, as well as other documents, no later than three business days before the date specified in the public offer for the release of tokens. Such tokens may not be offered to anyone or advertised prior to publishing the public offer.³⁰

The Draft Law sets forth a monetary limit beyond which unqualified investors (as defined in the Federal Law of the Russian Federation ‘On the Securities Market’)³¹ may not invest in tokens.³² Incidentally, the Azerbaijani equivalent of the above-mentioned Law, the Securities Market Law,³³ contains a definition of institutional investors, which also draws parallels with its Russian counterpart.

VII CONCLUSION

The absence of specific regulations on virtual currencies and their underlying technology in Azerbaijan may contribute to uncertainty and potentially stifle innovation in their implementation. For this reason, and in the interest of encouraging innovation in this sphere, the adoption of a separate law (along the lines of the Russian precedent discussed above) would be, in our view, a welcome legislative development.

25 Id., Paragraph 14, Article 2.

26 Law of the Republic of Azerbaijan ‘On the Securities Market’, No. 1284-IVQ, dated 15 May 2015, Republic of Azerbaijan Collection of Legislation 2015, No. 07, Item 813 (in Azerbaijani) [Securities Market Law]. Available at <http://e-qanun.gov.az/framework/30333>.

27 Law of the Republic of Azerbaijan ‘On Electronic Trade’, No. 908-IIQ, dated 10 May 2005, Republic of Azerbaijan Collection of Legislation 2005, No. 07, Item 564 (in Azerbaijani). Available at <http://e-qanun.gov.az/framework/10406>.

28 Law on the Prevention of the Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism, Article 9.

29 Draft Federal Law on Financial Digital Assets, Article 3.

30 Id., Article 3.5.

31 The Federal Law of the Russian Federation ‘On the Securities Market’ No. 39-FZ of 22 April 1996.

32 Id., Article 3.1.

33 Securities Market Law, Article 1.0.7.

A great deal of care should be given to striking the correct balance in regulating virtual currency-related activities and providing clear guidance to market players, while at the same time avoiding unintended consequences of overzealous regulation, which is a difficult, but not impossible, task. It remains to be seen if the Azerbaijani regulators will take up this challenge any time soon.

ABOUT THE AUTHORS

ULVIA ZEYNALOVA-BOCKIN

Dentons

Ulvia Zeynalova-Bockin is counsel in the Dentons' Baku office. Her practice includes banking law, Islamic finance, real estate finance, mergers and acquisitions, as well as corporate law and finance. Ulvia also has experience in securities and financial regulation, including work with the Corporation Finance Division of the US Securities and Exchange Commission in Washington, DC, and advising clients with business interests in the CIS countries while working in Salans' New York office and, more recently, at Dentons Rodyk in Singapore.

She has provided legal support to local and international clientele in high-profile matters, including the first IPO to be listed on the Baku Stock Exchange, advising major investment banks on the enforceability of ISDA master agreements, global master repurchase agreements and global master securities lending agreements, and participating in the privatisation of the largest bank in Azerbaijan. Ulvia has also successfully represented local and foreign banks in regulatory approvals and other business concerns.

She has been ranked as a 'Next Generation Lawyer' by *The Legal 500 EMEA* in 2017 and 2018 and as a 'Recognised Practitioner' by *Chambers and Partners Asia-Pacific 2018*.

DENTONS

8 Izmir Street
Hyatt International Center
Hyatt Tower 2
Baku, 1065
Azerbaijan
Tel: +994 12 4 90 75 65
Fax: +994 12 4 97 10 57
ulvia.zeynalova-bockin@dentons.com
www.dentons.com

Law
Business
Research

ISBN 978-1-912228-77-5