Lawyers Discuss 'What's Next' After China Shuts Down Cryptocurrency Exchange

'Many industry people believe the government's ban will effectively extinguish the hope that China becomes a global center of cryptocurrency,' attorney Pinghsan Li said.

Ed Silverstein, Law Technology News

September 20, 2017

China is shutting down Bitcoin and cryptocurrency exchanges, and attorneys familiar with cryptocurrency issues suspect the bans may have far-reaching consequences. This cryptocurrency ban comes when cryptocurrency transactions are reportedly at their peak in China and follows an earlier ban on token sales.

Why the Ban?

When asked about the move, Joshua Ashley Klayman, an attorney at Morrison & Foerster, told Legaltech News that China "appears to have expressed the same sorts of concerns that many other countries have raised—the prevalence of fraud and scams, anti-money laundering and related concerns, and certain tokens being securities but not being in compliance with the regulatory framework."

"China may have pressed pause on token sales and cryptocurrency exchanges in order to investigate and punish potential malfeasance, and to drive bad actors and other non-compliant parties from China's token space," Klayman further explained. "It's also possible that they may be halting the activities with a view to later allowing token sales and token exchange activities to resume, albeit in a more closely supervised and regulated manner."

She noted that it makes sense for the Chinese government to take further steps to force the shutdown of cryptocurrency exchanges "for example, in order to freeze tokens in place while it undertakes investigations of the tokens and token sales, particularly if the Chinese government may be trying to trace or track illegal activity."

"In addition, if some tokens are securities that had not complied with Chinese regulatory requirements, then the Chinese exchanges that facilitated the trading of those security tokens may have failed to comply with regulatory requirements," she explained. "It is possible that China's reactions may indicate just how much improper and non-compliant activity was taking place in China."

Vincent (Trace) Schmeltz III, an attorney at Barnes & Thornburg, speculated that China may have implemented the recent ban "to protect the yuan from the inflationary impacts of increased trading by Chinese nationals in cryptocurrencies. China has long rattled its regulatory sabre against cryptocurrencies, with the Chinese central bank speaking out early against them."

What It Means Practically

As far as the ban's impact, other jurisdictions may become more popular destinations for token sales and exchanges and fill the void that China's token-related bans may have created.

"Many industry people believe the government's ban will effectively extinguish the hope that China becomes a global center of cryptocurrency," Pinghsan Li, an attorney at Thompson Hine, said in a statement to Legaltech News.

Klayman agreed, adding, "Already, cancellations of cryptocurrency-related conferences have been reported, and potential token issuers have indicated that they had cancelled previously scheduled trips to meet with potential investors. China's role as a token hub of sorts may have been diminished, but it ultimately may become a safer jurisdiction for token investors if China ultimately decides to let token sales resume. There have been some suggestions that China could block access to overseas Bitcoin exchanges, in addition to the local ban. In addition, some have expressed concerns that China might consider putting a stop to Bitcoin mining."

Schmeltz further explained that the ban will deprive Chinese nationals of a non-government controlled currency, may "fan the passions of a middle class that sees cryptocurrencies as its way to escape the government's autocratic control over the yuan," and will deprive tech-developers of their ability to raise foreign investments for their projects.

Looking at the larger picture, China's move is likely to have an impact on international regulations, Klayman said.

"China has been a powerful player when it comes to token sales and exchanges. While China's reaction to token sales may have been more forceful than that of numerous other countries that have provided guidance regarding token sales and exchanges—including the United States, Canada and other jurisdictions—China also may have been [seeing] a heightened level of criminal behavior and non-compliance. It is possible that other jurisdictions that may have a high proportion of bad actors and illegal token activities may take an approach that is similar to China's."

But at the other end of the spectrum, she added, "Certain other jurisdictions may see China's bans as providing an opportunity for such jurisdictions to attract token sale and exchange business by providing light-touch regulation. While not an impact on international regulations, the Chinese bans have been blamed partially for the recent dips in the prices of certain cryptocurrencies—including Bitcoin—supporting the idea that the actions of one jurisdiction may be felt across the globe."

Similarly, Li said that “many other countries may rethink about their general policy towards cryptocurrency. On the other hand, there may also be other countries, especially some of the Asian countries that may want to take advantage of the vacuum left by this complete ban.”

As far as practical advice to businesses, Schmeltz recommended that any business “contemplating an initial coin offering, or that operates a crypto-exchange, ought to make sure it blocks Chinese IP addresses. With that said, this is likely the first step in a longer strategy by the Chinese government. Accordingly, after halting any on-going trading with Chinese investors, businesses ought to hold tight for now, and see what Chinese regulators do next.”