

Ban of Cryptocurrencies in China and Judicial Practice of Chinese Courts

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There are different approaches worldwide on how to regulate cryptocurrency: legalization, partial ban, or absolute ban. China has chosen the third option. Since 2013 the PRC has been introducing restrictive measures targeting ICO, Bitcoin and other cryptocurrency activities. In 2022 it finalized the formation of a legal framework for cryptocurrency regulation by publishing “Judicial Interpretation on Illegal Fundraising Criminal Cases.” The main reasons for the prohibitive Chinese approach are combating money laundering, ICO related scams, and illegal financing, i.e., public interest prevails over private interests. An analysis of the judicial practice of Chinese courts demonstrates that despite a rising number of cryptocurrency related civil disputes, plaintiffs are deprived of judicial protection because investing in digital financial assets is illegal and the rights of investors are not legitimate. The paper argues that a cryptocurrency ban makes it impossible to satisfy claims concerning illegal fundraising activities, while encouraging investors not to have any relations with illegal agents, brokers or exchanges.

Keywords: Peoples Court of China, Bitcoin, Cryptocurrency, Money Laundering, ICO

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1. Introduction

Cryptocurrencies and digital tokens are symbols of the modern financial sphere. Their specific features, such as anonymity and the unregulated character of transactions, have made them extremely popular for the Internet users and caused their rapid development in the last decade. Many types of cryptocurrencies, even including fake cryptocurrencies,¹ have appeared in the world. In 2020, their total number was estimated at 6,500 with a market capitalization of around USD 350 billion.² The most popular cryptocurrencies are Ethereum and Bitcoin, which have even turned into an underlying asset for crypto-futures.

Following the on-going instabilities associated with the Covid-19 pandemic, global economic crisis, geopolitical processes, and the escalation of military conflicts, a positive effect has been made on cryptocurrencies, in particular Bitcoin. Private and institutional investors, trying to save their money, have decided to diversify their traditional portfolio consisting of securities, bonds and cash, by investing in digital financial assets. Scholars noted that “by doing this, the invested is assured of escaping the potentially harmful effects resulting from placing all their eggs in one basket.”³ As a result, during the Covid-19 pandemic, Bitcoin has shown a dramatic rise in value and by the end of 2021 had reached a price of about USD 64,000. In March 2022, however, Bitcoin’s exchange rate fell to USD 38,000.⁴ This instability demonstrates the high volatility of cryptocurrencies, with all the positive and negative consequences. Therefore, cryptocurrencies are extremely risky for individual investors inexperienced.

The rapid growth of digital technologies in the financial markets has brought the sphere of investments to be far ahead of the development of legislation. Also, it has put before the governments and monetary authorities of different states the question of how to regulate activities with cryptocurrencies and fundraising via the procedure of Initial Coin Offering (ICO). In addition, as cryptocurrencies are out of sight of the states and used as an alternative to the traditional monetary system for making transactions on the Internet including cross-border ones, the free exchange of digital financial assets by fiat money has become more important.

Cryptocurrencies would hide the identity of its owners, which turns them into a means of payment for illegal activities such as the weapons trade, narcotics trafficking, etc. However, this anonymity of cryptocurrency users is not always

absolute in some states and therefore does not grant a safe haven for its owners. In February 2022, the US arrested a couple accused in laundering cryptocurrency that was stolen during the 2016 hack of Bitfinex.⁵ Whether or not cryptocurrencies really guarantee anonymity for its holders has become even more topical after the US based crypto-exchange Coinbase decided to block more than 25,000 cryptocurrency wallets of Russian citizens for political reasons in March 2022.⁶

Although cryptocurrencies and digital tokens have many payment and investment opportunities, they are dangerous for not only unsophisticated investors, but also a state. In this regard, ICO and cryptocurrencies should be regulated by legislation or provisions issued by monetary authorities. Otherwise, the contradictory nature of cryptocurrencies can harm the financial market. Unfortunately, there is not any worldwide legal framework adopted for cross-border ICO and cryptocurrency activities.

Despite all the advantages of digital financial assets, the Peoples Bank of China (PBOC) prohibited any transactions with Bitcoin in 2013⁷ as well as ICOs in 2017.⁸ Moreover, since March 1, 2022, any transactions with Bitcoin in the PRC have been considered a criminal offense.⁹ In comparison with the leading economies of East Asia, this position is unique. For example, Japan¹⁰ and Singapore¹¹ recognized cryptocurrency as a means of payment and supervise crypto-exchanges. They also declared that ICO should be regulated in accordance with legislation on securities and futures. In September 2018, Hong Kong authorities announced that “Bitcoin is not a means of payment and could not be qualified as a regulated asset,”¹² but digital tokens issued via ICO, if they fall under the scope of the Hong Kong Securities and Futures Ordinance,¹³ are assets which are regulated by the Hong Kong Securities and Futures Commission in accordance with the “Statement on Regulatory Framework for Virtual Asset Portfolios Managers, Fund Distributors and Trading Platform Operators,”¹⁴ and “Regulatory Standards for Licensed Corporations Managing Virtual Asset Portfolios.”¹⁵ As noted, there are many different strategies concerning regulation of digital financial assets.

The research aims to analyse the prohibition on ICO and cryptocurrencies in the PRC through examining its judicial practice. The decisions of the Chinese courts demonstrate the consequences of implementing restrictions and indicate the impact of the ban on crypto-exchanges, financial institutions, and private investors as well the protection of their rights. The outcomes of this research could be useful for

future discussions concerning the construction of a cross-border framework for cryptocurrency and ICO regulation.

This paper is composed of six parts including an Introduction and Conclusion. Part two will give a brief overview of ICO and cryptocurrency and illustrate challenges raised by digital financial assets. Part three will briefly describe the experience of different jurisdictions concerning the ban of ICO and cryptocurrency. Part four will be devoted to the analysis of Chinese legislation and notices of the PBOC about ICO and cryptocurrency. Part five will discuss the judicial practice of Chinese courts and indicate the main problems for protecting the rights of investors in the sphere of disruptive technologies.

2. Cryptocurrency, ICO and its Challenges

A. Cryptocurrency: Brief Overview

Bitcoin is the most popular cryptocurrency. It was presented in 2008 by Satoshi Nakamoto in his White Paper.¹⁶ Bitcoin is designed on the basis of a distributed ledger technology, which has specific features: consensus-driven, decentralization, transparency, and immutability.¹⁷ The feature of Bitcoin that makes this commodity popular among investors is anonymity of the person engaged in transactions. Unlike bank accounts and most other payment systems, Bitcoin addresses are not tied to the identity of users at the protocol level. Anyone can thus create a new randomly generated Bitcoin address (and the associated private key) at any time without having to provide anyone with personal information.¹⁸

Decentralization is the key characteristic of all blockchain based cryptocurrencies. It means that all participants of the Bitcoin network are equal with common access to transaction recordings and an awareness of all that is happening at a particular time. Additionally, no one can stop the transaction process or reverse it. Thus, decentralization leads to a high level of transparency between parties and makes it possible to provide B2B, B2C and P2P without a trusted third party which is usually a financial institution.

This being the case, the Bitcoin network could be accepted by parties as a means of payment and create a potential threat to the banking system.¹⁹ At the same time, the rapid growth of Bitcoin rates in conjunction with its high volatility has turned it

into an investment commodity²⁰ and decreased its function as a means of payment.²¹ Supporters of cryptocurrencies use them for investments because they can serve as a means of accumulating wealth against the backdrop of ever-increasing inflation. In any case, those cryptocurrencies as Bitcoin, Ethereum, etc., still have their potential to be means of payment.

B. Initial Coin Offering

The main idea of ICO is to attract funds to a special project. Accordingly, ICO is a fundraising model, where cryptocurrency is used as a means of financing. Although investors do not receive any rights to the company as in classical investment transactions, they may have rights to software protocols, goods, services, or those similar to shareholders or creditors. An ICO is implemented in the form of a preliminary issue of its cryptocurrency (tokens) and the distribution of tokens among interested parties.²²

ICO deals with two types of digital tokens: security tokens and utility tokens. Security tokens by their legal nature are close to securities giving their holders rights similar to corporate rights. Utility tokens include those that provide their owner an access to a platform service or application, the ability to purchase a product (product), etc.²³

In 2017, ICO was an extremely popular tool for investment activities because of its unregulated nature. According to the CoinSchedule website, which tracks information about the sale of digital tokens, in 2017, the total amount of funds raised by ICO amounted to USD 3,700,682,293, compared to USD 96,389,917 in 2016.²⁴ In 2018, the ICO market was in crisis, due not only to the fall in the exchange rate of key cryptocurrencies, but also to the lack of proper legal regulation and the fraudulent nature of the projects attracting investments.²⁵ Since 2019, however, a new type of ICO-Initial Exchange Offering (IEO) has become popular, where a crypto-exchange participates in the offer of tokens. The advantages of this type of fundraising include: high-quality selection, a professional audit of projects by the crypto-exchange, a guarantee that the project is not a scam, and the presence at the exchange of already targeted investors ready to buy tokens.²⁶

C. Challenges Raised by Cryptocurrencies and ICO

The unregulated character of ICO and decentralization as a cornerstone of the cryptocurrency system makes digital financial assets extremely popular for criminals²⁷ who use them in their illegal activities on the Internet.²⁸ Without clear legal regulation, cryptocurrency has been subject to manipulations by sophisticated investors all around the world.²⁹ Researchers noted that there are technological risks of investing in cryptocurrency³⁰ which makes them not a safe haven, but rather amplifiers of instability in financial markets.³¹ Moreover, popularity of cryptocurrencies among individuals, their belief in easy money, and a global economic crisis caused a massive influx of inexperienced investors in trades with cryptocurrencies.³² Due to the lack of official information and experience,³³ individuals would invest in crypto-projects primarily based on the blind trust in aggressive announcements of ICO initiators within social-media.³⁴

The indicated obstacles jointly have provoked an increase in fraud related to cryptocurrencies and ICO,³⁵ and cryptocurrency related scams rapidly diffused throughout the Internet. The frauds in the crypto-market is based on the promising high-profits due to the different exchange rates of cryptocurrencies, new investment strategies, and investment opportunities in new technological projects.³⁶ Nowadays, crypto scams could be divided into three main groups: fake (non-existent) cryptocurrencies and fake crypto-exchanges; ICO based financial pyramids and “Ponzi” schemes; and price manipulation and bubbles on the crypto exchanges.³⁷ The Covid-19 pandemic gave additional impetus to generating crypto scamming such like ICOs for vaccine of Covid-19, Covid-19 Crypto Malware, Covid-19 Crypto Blackmail, Covid-19 Fake Crypto Donation, Covid-19 Token Scam CoronaCoin.³⁸

A good example of a fake crypto-exchange is the Korean BitKRX³⁹, which did not provide trading with cryptocurrencies, instead just collected money. Some scammers created fake cryptocurrencies such as “My Big Coins,”⁴⁰ OneCoin, and CoronaCoin that cannot be exchanged for Bitcoins without any cryptocurrency features at all. Fake cryptocurrencies and pseudo crypto-exchanges are a real threat for unsophisticated investors subject to the uncontrolled advertisements in social media. The originators of OneCoin deceived about 3.6 million people and stole more than Euro 4 billion.⁴¹

A Ponzi scheme is a hierarchical investment system where a fraudster does

not realize any project, but simply generates high profits by attracting funds collected from new investors. This means that investors receive income only from contributions of newly recruited participants. This scheme could work for a long time only if new investors are constantly attracted. If investors simultaneously decide to demand payment of their gains or if the flow of newcomers slow down, the Ponzi scheme would collapse.⁴² A typical example of a Ponzi scheme in the cryptocurrency market is the case of the New York Bitcoin Savings and Trust cryptocurrency exchange which collected 146,000 Bitcoins amounting to about USD 5.6 billion (as of February 2022 rates). The exchange assured investors that it lent their Bitcoins to other persons and promised weekly gains at the rate of 7%, but in fact founders of the exchange simply embezzled cryptocurrency.⁴³ Chinese scholars detected more than 835 Ponzi schemes running on Ethereum with over USD 17 million invested by victims⁴⁴ and proposed different methods on how to detect them.⁴⁵

The extremely volatile character of cryptocurrencies makes their market vulnerable to scams like “pump-and-dump,” where scammers choose an exchange and a cryptocurrency, the value of which will artificially inflate. Organizers of the scam start pumping the price of a cryptocurrency on a particular exchange. In this course, due to a large influx of funds unsophisticated, investors start buying this digital financial asset, and when the price peaks organizers sell the asset at the inflated price, a ‘dump’ occurs and its value collapses in the end.⁴⁶ More frequently, price manipulations are occurring at newly established or unlicensed exchanges with a poor system of control.

Thus, cryptocurrencies have opened the door for different illegal actions, giving new opportunities for the Internet scams.⁴⁷ Obviously, this has caused a harsh reaction from the public authorities of states. Some of them have implemented a complete or partial ban on cryptocurrencies and ICO.

3. Ban of Cryptocurrency and ICO Prohibition

A. Prohibition of ICO and Cryptocurrencies

About 60 states all around the world have restricted the use of cryptocurrency.⁴⁸ Some states have prohibited the usage of cryptocurrencies as a means of payment

(i.e., a person is not allowed to use it instead of money, but may hold it and invest with it), while others have totally banned cryptocurrency and ICO on the premise that all these activities concerning cryptocurrencies are considered illegal. Although some states have not declared cryptocurrencies and ICO to be illegal, but stressed a need for investors and financial institutions not to use it. For example, according to the State Bank of Pakistan, “the General Public in their own interest is advised to be cautious of and refrain from indulging in activities relating to mining, trading, exchanging, transferring value, promoting and investing of Virtual Currencies/Coins/Tokens to avoid any potential financial loss and legal implications.”⁴⁹

There are three groups of states restricting ICO and cryptocurrencies: the first group allows usage of cryptocurrency and ICO but prohibits financial institutions from dealing with it; the second one treats cryptocurrency as an investment commodity and at the same time prohibits it as a means of payment; and the third one prohibits all transactions with cryptocurrency.

B. Ban of Cryptocurrency as a Means of Payment

Cryptocurrencies are not legal tender or a means of payment in more than 50 jurisdictions.⁵⁰ Also, some countries are on the way to prohibiting circulation of Bitcoin as a means of payment. In January 2022, the Bank of Thailand published a statement that it is going to limit the use of cryptocurrency as a means of payment.⁵¹ Monetary authorities of the states where this restriction is implemented proclaim that turnover of cryptocurrencies entails a violation of financial and monetary legislation. Central banks of these states warn against making payments with cryptocurrency and indicate that it is illegal from the viewpoint of financial legislation, as well as dangerous for its owners since it is not secured by anything. In Indonesia investing in crypto assets is allowed, but cryptocurrencies cannot legally be used for payments.⁵² In Vietnam, the Central Bank has even issued an official notice that the turnover of cryptocurrencies is equivalent to the issuance and use of illegal means of payment which finally constitutes a crime.⁵³ The Central Bank of Vietnam, however, did not declare investing with cryptocurrency illegal. It means that people may not make payments, but could invest in Bitcoin, Ethereum, etc.

The named positions of financial authorities are mostly connected with the threat of money laundering, terrorist financing, and sustainability of the financial system. Nowadays, it is doubtful that citizens use Bitcoin instead of money on the Internet

to pay for ordinary goods and services. The high volatility of cryptocurrency makes its utilization too unpredictable and therefore dangerous. Meanwhile, the cautionary steps of central banks are necessary to prevent individuals, companies and banks from supporting risky actions hitting monetary system.

C. Absolute Ban

Among the 51 states restricting cryptocurrencies, there are only 10 jurisdictions (including the PRC and Macao SAR) which have prohibited all operations with cryptocurrency, all of them being situated in Asia and Africa.⁵⁴ In Asia, cryptocurrency is prohibited in the PRC, Bangladesh, Iraq, Qatar, Oman and Nepal. In Africa cryptocurrencies are outlawed in Algeria, Egypt, Morocco and Tunisia. For example, according to the Bank of Bangladesh, the use of cryptocurrencies encroaches on financial and anti-corruption legislation, so that persons who carry out transactions with it are subject to prosecution.⁵⁵ The Central Bank of Iraq underlined that parties engaged in cryptocurrency activities should be punished under money laundering laws.⁵⁶ The Qatar Central bank prohibits all banks from dealing with Bitcoin, exchanging it with another currency, opening an account to deal with it, or sending or receiving any money transfers for the purpose of buying or selling this currency.⁵⁷ The same position has been taken by the Central Bank of Oman.⁵⁸ The Central Bank of Nepal announced that strict measures should be taken against persons trading in cryptocurrencies.⁵⁹ In Tunisia, cryptocurrencies are not officially banned, but in fact all transactions involving them constitute a crime.⁶⁰ According to Algerian Finance Law, any transaction with cryptocurrency will be punished as a financial crime.⁶¹ In Morocco, activities with Bitcoin constitutes an infringement of foreign exchange regulations,⁶² punishable by penalties and fines.⁶³ A quite interesting situation is in Egypt. Here, not only the Central Bank has restricted trading in cryptocurrency,⁶⁴ but also religious authorities have issued a Fatwa that forbids Bitcoin⁶⁵ because it contradicts the principles of Islamic banking, from the viewpoint that transactions with cryptocurrency is gharar – excessive uncertainty. So in Egypt, cryptocurrency is under a double prohibition. Notably this situation is not unique, with similar prohibitions in other states where Sharia law is implemented.⁶⁶

It seems that the cryptocurrency in the above-mentioned countries is banned because their public bodies have neither developed, nor introduced a mechanism allowing the supervision of the crypto-investment sphere and crypto-exchange

activities. That is why the authorities have decided not only to protect public interests concerning monetary system, but also to reduce the risks for retail investors from cryptocurrencies which do not have a basic generated asset.

4. Cryptocurrency and ICO Prohibition in the PRC

A. Overview of Cryptocurrency and ICO Regulations in China

China started the struggle against cryptocurrencies in 2013 when the PBOC published the Notice on Precautions Against the Risks of Bitcoins.⁶⁷ The Notice prohibits financial institutions from making any transactions with Bitcoin and empowers the Anti-Money Laundering Monitoring and Analysis Center with tracking all suspicious bank transactions related to cryptocurrencies. In addition, the Notice has an important guiding value for money laundering control. It does not suppress innovation, but supports transparency of information and allows fighting crime.⁶⁸ The main reason why the PBOC took such a strict position is that Chinese criminals use Bitcoin to legalize their illegal gains with the help of trading platforms⁶⁹ or Bitcoin Vending Machines⁷⁰ providing exchange services.

In 2017, the PBOC prohibited ICO,⁷¹ stressing that financing token issuance is an act of illegal public financing which constitutes financial fraud. Some researchers have criticized this policy. They believe that digital tokens could be regulated similar to securities.⁷² Meanwhile, digital tokens do not always constitute a share in a company, so that it is incorrect to treat all digital financial assets in accordance with securities legislation. Also, Chinese officials seem to have decided that ICOs are just tools to show how not to fulfill requirements for an initial public offering⁷³ because only less than 1% of ICO projects use the financing funds for project investment.⁷⁴

In 2018, Chinese authorities issued the Notice on Risk Warning against Illegal Fundraising in the Name of “Virtual Currency” and “Blockchain.”⁷⁵ This document explains how criminals promote illegal fund-raising by ICOs, IFOs and IEO; and mislead investors by offering intermediary services and attracting funds under the name of overseas high-quality blockchain projects. Thus, this Notice discloses the various tricks used for fraud and refers to ICO as a kind of financial pyramid, giving

a number of such examples.⁷⁶ Also in 2018, the Business Management Department of the PBOC issued the Notice on Carrying out Self-Inspection and Rectification of Payment Services for Illegal Virtual Currency Transactions,⁷⁷ which requires all payment institutions to carry out self-inspection and strictly prohibits providing any services for virtual currency transactions.

The latest Notice concerning cryptocurrencies and ICO was issued in September 2021 by the PBOC and nine other authorities.⁷⁸ This Notice improves on the provisions issued previously; establishes requirements to a risk prevention system; and shapes a finalized legal framework for ICO and cryptocurrency. In this course, the Supreme People's Court and the Supreme People's Procuratorate participated in developing this Notice, because it is based on their experience connected with the counteracting challenges raised by digital financial assets. Therefore, this document could be counted as a guideline to personnel of the law enforcement system. Article 1 of the Notice on Further Preventing and Resolving the Risks of Virtual Currency Trading and Speculation gives characteristics of cryptocurrencies specifying that Bitcoin, Ethereum, Tether, and other digital financial assets are not legal tender, and thus should not and cannot be circulated as currency in the market. The Notice proclaims all cryptocurrency-related activities, including those carried out by foreign cryptocurrency exchanges, illegal; indicates them as a financial crime; and establishes a rule that investments in cryptocurrencies are not legally protected.

Besides the notices of the PBOC and governmental bodies concerning cryptocurrency related transactions, provincial authorities are empowered to regulate Bitcoin mining. In May 2021, for example, Inner Mongolia established the Virtual Currency Mining Enterprise Reporting Platform⁷⁹ targeting to close all 'mining' projects in the region. Sichuan Province, which was the world's largest location of Bitcoin miners, announced in June 2021 the closure of 26 virtual currency mining projects on its territory by issuing a Notice on the Cleanup and shutdown of virtual currency 'mining' projects.⁸⁰

In this regard, there were four steps concerning the crackdown of digital assets in China: a ban of Bitcoin in 2013, prohibition of ICO in 2017, a ban of all cryptocurrencies, and the shutdown of mining farms in 2021. China introduced its measures step by step, meaning that Chinese officials decided not to rush but to analyze the consequences of their decisions. From one side, it is not good for new activities because they could end up in a grey zone, while, from the other side, it

helps to elaborate an appropriate regulatory approach. The prohibitive approach used in China is criticized by some scholars as leading to the gray development of digital currency in the private sector⁸¹ and restraining financial innovations,⁸² or directly marked as inefficient.⁸³ However, it does have objective reasons such as reducing the level of capital outflow, preventing money laundering and illegal fundraising, protecting investors from fraudulent activities, and supporting rational electricity usage.

B. Legal Liability for Cryptocurrency and ICO Related Activities in China

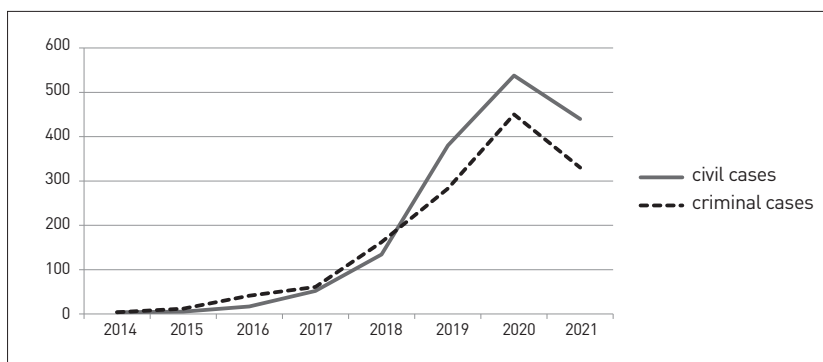
Due to the cryptocurrency ban, the price of Bitcoin increased, consequently stimulating Chinese investors to deal with digital assets by the agency of local speculators, who then spread information about illegal intermediary platforms through social networks, WeChat and QQ. This scheme is very burdensome for investors because the safety of their assets is not guaranteed. If a foreign cryptocurrency exchange for any reason takes away Bitcoins or goes bankrupt, the funds will not be returned to the Chinese investor. In 2019, for example, Gao was accused, together with accomplices, of exploiting foreign servers to advertise his services concerning Bitcoin storage and management, guaranteeing customers the opportunity to receive gains from 1/1000 to 8/1000 percent daily. The platform was soon closed, and investors lost access to their funds with an amount of up to CNY 15 million.⁸⁴

In order to realize the ban, Chinese authorities had to introduce a mechanism for prosecuting a person who committed cryptocurrency related activities and punishing them with administrative penalties. In February 2021, the PRC State Council enacted Regulation on the Prevention and Treatment of Illegal Fund-raising.⁸⁵ According to Article 30 of the Regulation, illegal fundraisers shall be fined not less than 20% but not more than the total amount of funds raised; persons who are directly responsible for illegal fund-raising shall be fined up to CNY 5 million; and if the fund-raiser is an organization, its business license shall be revoked. Article 31 of the Regulation establishes liability for persons who assist in illegal fund-raising. Moreover, Articles 34 and 35 lay down liabilities for advertising operators (advertising publishers) and the Internet service providers who failed to check information about a fund-raiser and for financial institutions or non-bank payment institutions, respectively. Hereby, the persons liable for ICO and cryptocurrency offences are: fundraisers and their personnel, their assistants (brokers, agents,

etc.), and their services providers (financial and payment institutions, advertising operators, and the Internet companies). As the Chairman of China Banking and Insurance Regulatory Commission, Guo Shuqing noted that the Regulation would help officials pay close attention to new types of risks under the banner of blockchain, virtual currencies and illegal fund-raising that infringes the interests of vulnerable groups.⁸⁶

If a person engaged in cryptocurrency related activities in China causes significant harm, s/he will be punished in accordance with the PRC Criminal Law. In 2020, a Chinese court sentenced the ringleaders of a cryptocurrency-based pyramid scheme, which had its servers located overseas, to 11 years in prison after they defrauded about 60,000 investors out of USD 2.25 billion. This case shows that China's officials have serious intentions to crackdown on cryptocurrency-related financing activities.⁸⁷ Notwithstanding, Chinese scholars noted that the ban of cryptocurrency related activities demonstrates that China's Criminal Law is not sufficient to resist digital currency crimes, so that amendments to the Criminal Law and judicial interpretations are needed.⁸⁸ Indeed, from 2014 to 2020, the quantity of cryptocurrency related lawsuits rose significantly, but since 2021, the number of civil cases decreased by 18% and criminal cases by 26,6%. It could be interpreted as a consequence of successful implementation of the state measures to counteraction against illegal fundraising.

Figure 1: Dynamics of Cryptocurrency Related Cases in the Chinese Courts⁸⁹



Source: Compiled by the author.

Despite the declining cryptocurrency related cases, the Chinese authorities keep strengthening their struggles against the crimes. In March 2022, the Supreme People's Court enforced Interpretation on the Specific Application of Law in the Handling of Criminal Cases about Illegal Fund-raising.⁹⁰ According to Articles 2 and 7, anyone who illegally absorbs funds through virtual currency transactions should be punished for the crime in accordance with the provisions of Article 176 of the Criminal Law.⁹¹ If a fundraiser uses fraudulent methods, s/he will be liable under Article 192⁹² of the Criminal Law.⁹³ In accordance with Article 9 of the Interpretation, the Supreme People's Court also guides on how to apply the Criminal Law to sentencing a person convicted of illegally absorbing public deposits.

Thus, the Chinese authorities regulate Bitcoin and ICO related activities very strictly by imposing a ban on any transactions with digital financial assets. In 2022, China finalized the formation of the legal framework for cryptocurrency and ICOs by enacting the Supreme People's Court's Interpretation which unambiguously proclaimed any transactions with cryptocurrencies and ICO as illegal fundraising. The PBOC and other Chinese public bodies stated that the key goal of investment token issuers is to bypass current legislation of financial markets and to attract funds into doubtful projects or directly to commit fraud.⁹⁴

C. Do Cryptocurrency Related Investments are protected in China?

In 2014-22, Chinese courts of all levels, including the Supreme People's Court, considered 2,968 cases related to cryptocurrencies, 54% of which were civil.⁹⁵ Notably, after 2017, the number of civil cases began to increase with lightning speed and then stopped in 2021 (Figure 1). Even so, civil cases are prevailing over criminal cases in Chinese courts. It demonstrates that there are more disputes from the contracts related to cryptocurrencies. Does this mean that the judicial system of the PRC is defending individuals investing in digital financial assets?

In order to answer this question, different awards on civil cases should be analyzed. For example, the intermediate People's Court of Sanya pointed out that since transactions with tokens are not legal, the citizens trading them must bear their own risks by themselves.⁹⁶ Similar awards are adjudicated by other courts. The decision of the intermediate People's Court of Hangzhou (China's digital capital) explains that individuals using the services of cryptocurrency brokers only have rights to create an account for the purchase of tokens and there are no obligations on

the side of broker, other than opening an account and transferring the virtual wallet activation code. If an investor did not receive the promised profits and asks for recovery, his/her claim may not be satisfied since the income from illegal activities cannot be judicially protected.⁹⁷ Meanwhile, as stated by the Intermediate-level People's Court of Guilin, investors have the freedom of investment and transaction of virtual currency because it is their private matter.⁹⁸

By these actions, Chinese courts are strongly encouraging citizens not to invest in digital tokens, but simultaneously they have stressed that national laws and administrative regulations do not prohibit cryptocurrencies from being purchased and held by individual citizens as commodities.⁹⁹ Despite the fact that individuals may own cryptocurrencies, the courts have concluded that investors cannot be protected by law and are refusing to satisfy investors' claims towards cryptocurrency exchanges and speculators.¹⁰⁰

Some courts not only deny protecting investors' rights, but also name contracts concerning ICO and cryptocurrency transfer as invalid. For example, the Intermediate People's Court of Wuxi indicated that a transfer of funds invested in virtual currency between the parties should be declared invalid due to its violation of the mandatory provisions of laws and administrative regulations.¹⁰¹ Other courts stressed that citizens investing in and trading virtual currencies have disrupted the country's financial administrative order, which has constituted a violation of public order and good customs, and is not protected by law.¹⁰² So, the subject matter of the transaction between the two parties in this case is an illegal circulating property.

Meanwhile, the Chinese judicial system protects citizens who receive cryptocurrency for their work. In June 2020, an overview of the practice of the courts of Shandong Province was published on the official account of the People's Court of the Highest Level of Shandong Province, including the case "On the contract dispute Ma Moumou v. Liu Moumou, Chang Mou, Li Moumou."¹⁰³ According to the award, although investing or trading in cryptocurrency is not protected by law, Bitcoins obtained in the process of a legal job are virtual goods which shall be transferred to a person, so that the contractual obligations are valid, legally binding and shall be protected.¹⁰⁴ This case has shown that possession of digital assets is judicially protected, but investment activities with the help of cryptocurrencies are not legal.

Thus, investments of individuals in digital financial assets are not protected in the PRC. Chinese courts neither recognize the interests of investors as legitimate,

nor encourage investment activities related to digital tokens. This approach is probably invoked to demonstrate that if individuals do not observe law, they could lose their money. However, this may encourage investors to use other jurisdictions. As the researchers rightly point out, the supervision or prohibition of digital tokens by the state cannot play a significant role in the regulation of ICOs as the investor will redirect the flows of his/her funds to the countries where activities with cryptocurrencies are legal.¹⁰⁵

5. Conclusion

A prohibitive approach is good for combating money laundering, but it could not stop investments in cryptocurrency. The crackdown of cryptocurrency related activities in China has inadvertently stimulated the rise of alternative over-the-counter channels for buying and selling digital financial assets. The global character of the Internet, in conjunction with different illegal or half-legal agent services, makes it possible for individuals to use foreign jurisdictions. Only the toughening of legal liability and denial of justice will help to decrease the number of cryptocurrency related trials. The Chinese experience shows that if a ban of cryptocurrency is applied, the main reason for individuals not to invest in digital financial activities is the threat of losing their money. In this case, a question may arise as to whether or not a complete ban on cryptocurrencies is worth losses that investors have suffered. In order to protect investors' rights and eliminate negative consequences of ICO scams for individuals, the only way is to launch a clear institutional framework legalizing cryptocurrency related activities, clarify the rights and obligations of the relevant subjects and state bodies, and effectively incorporate Bitcoin into the existing regulatory framework. If a state wants to prohibit cryptocurrencies, the Chinese scenario is recommendable to use. However, it is complex to implement such measures like prohibition of ICO and cryptocurrencies and their associated mining activities, adoption of judicial interpretation or legislation concerning legal liability of engaged persons in banned activities, and denial of justice for persons investing in digital financial assets.

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