

November 18, 2017

Japan Blockchain Association

Guidance for ICO Token Sales to Japanese Residents

There has been misconceptions about ICO sales in Japan such as that (i) Japan has no regulations on Initial Coin Offering (“ICO”) and/or, (ii) no Japanese laws apply if an entity is located outside of Japan, and (iii) thus a foreign entity can solicit Japanese residents to purchase ICO tokens without any restrictions. However, these comments are misleading and false.

We strongly recommend careful consideration of the Japanese regulations in soliciting Japanese residents to purchase ICO tokens in order to avoid potential punishment including a criminal penalty.

1 General Concept of ICO Regulation in Japan

Japan has no specific ICO regulations, and does not prohibit all ICOs. However, this does not mean Japan allows all ICOs. Existing financial regulations such as security and collective investment scheme regulations, and virtual currency or prepaid payment instrument regulations may apply to some kinds of ICOs. Even if those regulations do not apply, other laws such as civil law, commercial transaction law, consumer protection law, and criminal law would almost always apply to ICOs.

2 Careful Consideration is Necessary when Solicitation is Made

You need to carefully examine applicable laws when you try to sell ICO tokens to Japanese residents. Even if you reside in a foreign country, Japanese regulations still apply when you make a “solicitation” of certain kinds of products to Japanese residents. The term “solicitation” when you make sales via the Internet is broadly interpreted under Japanese laws. If offshore ICO issuers or sellers do not want to be regulated under Japanese laws when soliciting investors online, we strongly recommend that they shut out all Japanese residents from transacting on their site.

3 Warning from Japanese FSA

The Japanese Government’s Financial Services Agency (“FSA”) issued a warning on ICO on October 27, 2017. The FSA stated therein that if an ICO falls within the scope of the Payment Services Act (“PSA”) and/or the Financial Instruments and Exchange Act (“FIEA”), then “delivering such services without registration is subject to criminal penalties.”

Please see the below link:

http://www.fsa.go.jp/policy/virtual_currency/07.pdf

4 Examples of Applicable Regulations

Find below some examples of applicable regulations to ICO. They are not exhaustive.

(1) "Virtual Currency" Stipulated in PSA (called the VC Act)

- (a) If ICO tokens are deemed "Virtual Currency" ("VC") as defined in the VC Act, only registered Virtual Currency Exchange Business Operators are authorized to handle such ICO tokens.
- (b) Even a registered VC Exchange Business Operator is not authorized to handle all existing VCs. The VCs to be handled should be reported to and, as a matter of practice, approved by the FSA. _
- (c) The criminal penalty for conducting a VC exchange business without registration is imprisonment for 3 years or less and/or a fine of 3 million yen or less.

(2) "Prepaid Payment Instruments" Stipulated in PSA

- (a) If ICO tokens are deemed "Prepaid Payment Instruments" ("PPI") as defined in the PSA, registration with or notification to FSA is required depending on the type of PPI.
- (b) The criminal penalty to issue PPI without registration or submission of appropriate notice is imprisonment and/or a fine.

(3) Fund Regulation in FIEA

- (a) The fund regulations pursuant to the FIEA (the "**FIEA Fund Regulations**") will apply, if the ICO constitutes a "collective investment schemes (fund)," i.e., a scheme that is (i) to collect money from others; (ii) to invest in a business; and (iii) to pay dividends to holders thereof.
- (b) The seller of collective investment schemes is required to register as a Type II Financial Instruments Exchange Business Operator unless a certain exemption applies
- (c) The criminal penalty to solicit investors to a collective investment scheme without registration is imprisonment for 5 years or less and/or a fine of 5 million yen or less.

(4) Specified Commercial Transaction Act

- (a) If ICO tokens are not regulated under financial regulations such as the VC Act and FIEA, the Specified Commercial Transaction Act would generally apply to sales of ICO tokens

via the internet.

- (b) The Specified Commercial Transaction Act requires certain kinds of basic disclosure such as the name, address and telephone number of a person who is in charge of sales, price, payment method, limitation of warranty (if applicable), etc. Further, the Specified Commercial Transaction Act prohibits some acts such as an extravagant advertisement.
- (c) The criminal penalty for an extravagant advertisement is a fine of 1 million yen or less. If the person who makes an extravagant advertisement did not provide basic disclosure items, the penalty for that person will be imprisonment for 1 year or less and/or a fine of 2 million yen or less.

(5) Consumer Protection Act

- (a) From the general consumer protection point of view, an appropriate explanation to investors is required irrespective of whether or not such ICO tokens are regulated by the VC Act, by the FIEA or by the Specified Commercial Transaction Act.
- (b) The consumer can cancel the purchase of ICO tokens if there is a lack of appropriate explanation as required by the Consumer Protection Act.

EOD