# LEGAL REGULATION OF INITIAL COIN OFFERINGS IN RUSSIA

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*Abstract*

Depending on the country, the approach to Initial coin offerings (ICOs) may be different. While some jurisdictions are hesitating from regulating this industry, Russia has taken the lead and presented a specific regulatory framework for ICO's and blockchain technology. This article seeks to give an outline of the laws related to ICOs in Russia. In particular, there are discussed two main questions: whether Russian framework concerning 'blockchain' is a meaningful concept and whether there are regulatory rules which can be taken into account while elaborating global ICO regulation and which disadvantages should be avoided.

TABLE OF CONTENTS



## 1. Introduction

The development of the society is accompanied by constant changes. An actual phenomenon in the context of global digitalization is the development of the latest financial technologies (hereinafter-FinTech, fintech). Nowadays FinTech represents a new chapter in financial regulation that marks a break from past cycles of innovation. revolution assumes to provide a number of advantages for the economy, e.g. free access to capital, better investment assistance and more secure operations[1]. One of the main

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goal of fintech is to lower transaction costs in order to better allocate capital on the markets. They have proven the availability of receiving alternative sources of financing.

FinTech today comprises five major areas[2]:

1) Customer interface. Fintech technology allows customers to quickly access financial services and thereby simplify and automate their interaction. For instance, it offers customers greater mobility and ease of working with personal finance management systems, loans and transfers compared to banks.

2) Internal operations and risk management. The main task of risk management is to provide formalized information about the possibility of risk events and choose ways to deal with them. For example, SAS Risk Management (SAS), which is a widely recognized as worldwide solution in the field of risk management at the bank-wide level. Besides, EGAR Focus (EGAR Technology) is a comprehensive solution for banks and investment companies that allows to monitor positions, manage risks, evaluate the value of derivative financial instruments, and calculate profits and losses in real time.

3) Payments and infrastructure. Payment services occupy a major place due to their simplicity as financial products. The payment services for consumers include mobile wallets, direct payments between cards of different banks, currency exchange services (i.e., a cross-border transfer could be made by using the British services Kantox and TransferWise).

4) Data security. Due to digitalized nature, financial industry is vulnerable for cybercrime and espionage. In this regard much attention is paid to the information security of banking systems and protection of personal data in the Internet. For instance, information security methods such as multi-factor authentication and dynamic transaction confirmation have become mandatory.

5) Finance and investment concentrate on alternative financing mechanisms, specifically crowd funding and P2P lending. Crowdfunding means attraction of funds from a large number of users through a specialized Internet platform. P2P

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[1] *The Fintech Revolution*, The Economist (May 9, 2015), *https://www.economist.comlnews/leaders/21650546-wave-startups-changing-financefor-better-flntech-revolution* [*https://perma.cc/3FQW-UUZC*] (discussing benefits).

[2] D.W. Arner, J. Barberis, R.P. Buckley, *The Evolution of FinTech: A New Post-Crisis Paradigm*, 47 Geo. J. Int'l L. 1291 (2016).

lending as an alternative to bank lending provides direct interaction between borrowers and lenders/investors (including retail) without the mediation of a bank or other financial institution. Another alternative financing mechanism which attracts the attention of the public, investor, and regulatory is called initial coin offering (ICO).

ICO is one of the new ways of attracting investment through the sale of coins (tokens) to investors in the form of cryptocurrencies and crypto assets based on blockchain-financing mechanism. The «basics» of ICO are blockchain, smart contract and digital assets.

The main advantage of ICO is the use of blockchain technology – a decentralized digital transaction register. A blockchain represents a database that can be used simultaneously by many participants, each of them instantly synchronizes changes in it. The database is formed as a chain blocks containing a fixation of all transactions that are being performed, with each new record referring to the previous one. Due to the connection of all records with each other, it becomes impossible to forge one of them without changing the rest[3]. Typically, the key constituents of ICO process are fully automated by computer protocols on a blockchain, called smart contracts[4].

To sum up, ICO is based on blockchain infrastructure where tokens are placed, distributed and exchanged with the help of a smart contract without any intermediaries[5].

Initial coin offerings are a global phenomenon disrupting capital markets across several countries. As more offerings are held and more investors are enticed by promises of significant profits, a new regulatory framework becomes critical to promoting

[3] A.B., Brizitskaya, Y.S. Serebryakova, *Approaches to ICO regulation in the World economy*, Materials of the X I International student scientific and practical conference "Economic Sciences. Current state and prospects of development", 17-28 (2018), available at *https://www.elibrary.ru/item.asp?id=32644824.*

[4] M. Chanson, M. Risius, F. Wortmann, *Initial Coin Offerings (ICOs): An Introduction to the Novel Funding Mechanism Based on Blockchain Technology*, 24th Americas Conference on Information Systems 2018: Digital Disruption, AMCIS 2018, New Orleans, LA, 16-18 August 2018, available at https://espace.library.uq.edu.au/view/UQ:054eb24.

[5] S.L. Furnari, *Trough Equity Crowdfunding Evolution and Involution: Initial Coin Offering and Initial Exchange Offering*, 74 Lex Russica, 101 (2021), available at *https://cyberleninka.ru/article/n/trough-equity-crowdfunding-evolution-and-involution-initial-coin-offering-and-initial-exchange-offering*.

innovation without exploiting unsophisticated investors[6]. Given the amount of money involved, it is not surprising that most governments have looked at how they should approach crypto assets in general, and ICOs in particular. As should be expected, however, different jurisdictions have taken a wide variety of regulatory approaches to public distribution of these new phenomena[7].

The analysis of legal regulation of ICO and digital assets in different countries allows to classify States in three main groups: the State which on the legislative level stipulate a ban to conduct ICO and turnover of digital assets (Bolivia, Bangladesh, Brazil, Afghanistan, etc.); States, not officially prohibiting ICO, but not regulating this phenomena (Greece, Denmark, etc.); the State in which the legal framework governing ICO are already reflected in national legislation or positions of regulators (Malta, France, Germany, Liechtenstein, Switzerland, Japan, etc.).

At the same time, regarding the EU member states, it is necessary to take into account not only national regulation, but also supranational legislation of the European Union. Currently, the EU is working on common principles for crypto regulation for all member states. On 24 September 2020 the European Commission adopted a digital finance package. It includes a digital finance strategy and legislative proposals on crypto-assets for the EU financial sector providing consumers with the access to financial services and ensuring consumer protection[8]. This package is aimed at the EU's commitment to an economic recovery after coronavirus pandemic based on digital transition. It is expected that digital financial services can contribute to the modernization of the economy and transforming Europe into a global digital actor. By making the rules more digitally safer for consumers, the Commission seeks to exploit the synergy between newly established financial companies, eliminating the possible risks. Besides, the financial markets are regulated on the EU level by numerous regulations and directives. In particular, the European Securities Market Supervision Authority (ESMA) in 2017 defined

[6] N. Essaghoolian, *Initial Coin Offerings: Emerging Technology's Fundraising Innovation*, 66 UCLA L. Rev 294 (2019).
[7] C.R Goforth, *It's Raining Crypto: The Need for Regulatory Clarification When It Comes to Airdrops*, 15 Indian J. L. & Tech. 321 (2019).
[8] See *https://ec.europa.eu/info/publications/200924-digital-finance-proposals_en*.

the requirements for ICOs in the EU member state[9]. ESMA does not prohibit ICO in EU countries, but emphasizes that ICO projects should not contradict EU legislation. For instance, according to the EU Prospectus Directive, if the ICO project meets the criteria of an IPO (public offering of securities), it is necessary to publish a pre-approved by the regulator prospectus. Moreover, EU securities regulation is applicable to ICOs with the security tokens. In this respect the former Prospectus Directive[10] and the new Prospectus Regulation[11], the Market Abuse Regulation[12], and the MIFID II[13] form the core of financial legislation across the EU.

Broadly speaking, nowadays it is difficult to make blanket statements about clear ICO legal regulation because of the different regulatory schemes and approaches. But while some regulators struggle to keep up with the ICOs currently-existing regulatory regimes, Russia has already taken major stages of developing a clear regulatory paradigm for crypto assets. Moreover, Russia currently has one of the most up-to-date legislation regarding the regulation of the issuance and circulation of digital assets. For that reason, it is worthwhile worldwide to study Russian legal framework regarding ICO.

I will therefore try to draw conclusions on strengths and weaknesses of the Russian ICO framework and extract the positive elements which could be incorporated into a harmonised crypto-asset framework for adoption worldwide.

The research question addressed in this article can thus be formulated as follows:

What are the difficulties that may be encountered and solutions to them on the way of elaborating global approach towards ICO regulation on the example of Russian legislation?

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[9] See *https://www.esma.europa.eu/search/site/ICO*.

[10] Council Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading, amended by Council Directive 2010/73/EU on the prospectus to be published when securities are offered to the public or admitted to trading, OJ L 345, 31.12.2003, p. 64.

[11] Council Regulation (EU) 2017/1129 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, OJ L 168, 30.6.2017, p. 12.

[12] Council Regulation (EU) No 596/2014 on market abuse OJ L 173, 12.6.2014, p. 1.

[13] Council Directive 2014/65/EU on markets in financial instruments OJ L 173, 12.6.2014, p. 349.

The article begins in Part Two by examining the understanding of the fundamentals of legal regulation of ICO in Russia. Besides, to address the research question, it is important that the reader has a broad understanding of digital assets and its taxonomy. Meanwhile it is important to mention, that in Russia the legislator took a different path with respect to the global approach by introducing such concepts as "digital rights", "digital financial assets", "utility digital rights". Therefore, the Part Three briefly describes the classical approach to tokens as well as introduces the notion of digital rights, and its main types - digital financial assets and utility digital rights. Besides, the author highlights features of digital rights, the differences from the global approach to the digital assets. The Part Fourth deals with the determination of the law applicable to the issue of digital rights. Finally, the article briefly concludes about recommendations concerning possible future ICO regulatory developments on the international level.

## 2. The Russian model of ICO legal regulation

One of the essential questions in defining the most appropriate regulatory ICO approach is deciding whether crypto assets require completely new regulation or if they should be regulated in line with existing regulations. Russian model of ICO legislative regulation can be described as synthetic, since it combines new special rules regulating crypto assets as well as amendments to existing legislation.

The new legislative rules regarding crypto assets have been entered into force in the Russian Federation with the adoption of two federal laws, namely Federal Law "On Attracting Investments using Investment Platforms and on Amendments to Certain Legislative Acts of the Russian Federation"[14] (hereinafter - the Law on Investment Platforms) dated 02.08.2019 N 259-FZ and Federal Law "On Digital Financial Assets, Digital Currency and on Amendments to Certain Legislative Acts of the Russian Federation"[15] (hereinafter - the Law on DFA) dated 31.07.2020 N 259-FZ. Besides, amendments were made to the current legislation, in particular in the Civil code of the Russian Federation, Federal Law "On Countering the Legalization (Laundering) of proceeds

[14] РГ. 2019. N 172.
[15] RG. 2020. N 173.

from crime and the Financing of Terrorism" dated 07.08.2001 No. 115-FZ, Federal Law "On the Securities Market" dated 22.04.1996 N 39-FZ and some others.

It seems interesting to note the reasons for establishing a crypto assets regulatory framework in Russia. To a greater extent the adoption of the Federal Laws is a response to the requests of the economic community. Information technologies provide new opportunities for investing, raising funds necessary for business development. At the same time, there are new risks associated with the use of such technologies in the field of investment. It should be noted that the lack of a legal mechanism for investing in the digital economy significantly hinders its development and contributes to the expansion of the shadow sector. This, in particular, leads to the spontaneous spread of alternative financial instruments. But the reliability of such financial instruments raises serious doubts. By investing money in them, investors are deprived of guarantees of their return due to the lack of a legal mechanism that protects the rights of investors, as well as regulatory influence from government agencies. Their functioning outside the legal field prevents the implementation of the powers of the financial authorities of the state in this area (the Ministry of Finance of Russia, the Bank of Russia, etc.), provides an opportunity for illegal activities (concealment of income, financing of terrorism, etc.).

Furthermore, the President of the Russian Federation in his Message to the Federal Assembly in 2019[16] noted that it is necessary "... to promptly adopt laws that are priority for creating a legal environment for a new, digital economy, which will allow concluding civil transactions and attracting financing using digital technologies, developing e-commerce and services".

Besides, according to sub-item "p" of item 4 of Part I of the Strategy for the Development of the Information Society in the Russian Federation for 2017-2030[17] digital economy is an economic activity in which the key factor of production is digital data, processing large volumes and using the results of analysis of which, compared with traditional forms of management, can significantly improve the efficiency of various types of production, technologies, equipment, storage, sale, delivery of goods and services. Of great

[16] See *http://kremlin.ru/events/president/news/59863* (last access: Feb. 02, 2022).
[17] Decree of the President of the Russian Federation No. 203 of May 9, 2017 "On the Strategy for the development of the Information Society in the Russian Federation for 2017-2030", SZ RF. 2017. N 20. St. 2901.

importance for the economic development of the country is the formation of an ecosystem of the digital economy - a partnership of organizations that ensures the constant interaction of their technological platforms, applied Internet services, analytical systems, information systems of public authorities of the Russian Federation, organizations and citizens.

Overall, the development of legislation concern digital assets in the Russian Federation is stipulated primarily by promotion of market economy, because innovative activities can diverse business and income. Meanwhile, it is worth pointing out that consumers in Russia are left vulnerable as there exist no special legal rules to protect them. But the risks of clients conducting money are potentially high. Crypto asset trading platforms may not have special mechanisms to guard against fraud and hacking incidents. In addition, consumers are not sufficiently informed of the risk of crypto assets and the losses that can be incurred as a result of investing and trading in crypto assets.

Thus, the legal regulation of digital assets underlies the development of the Russian economy. And high hopes for the stability and viability of the Russian legal framework in relation to ICO have grown due to the adoption of the two abovementioned federal laws.

But it is the view of the author that new regulation at the federal level of the Russian Federation is clearly not enough for a ubiquitous application of blockchain technologies. It is stipulated by the size of the territory of Russia predetermines the large distances between the centers of economic activity, the presence of remote territories in the subjects of the federation, which generates significant inequality Therefore, in addition to federal legislation, legislation at the level of the states is also needed. It should contain norms that reflect the specifics of each subject. At the federal level, the basic principles of ICO regulation should be established, and the subjects of the Russian Federation, should have the right to independently exercise legal regulation in this area.

### 3. Digital rights as an object of civil rights

The technical basis of the ICO is a token, that could not be ignored when studying this technological phenomenon. Tokens along cryptocurrencies are the two most common blockchain-based digital assets. But it is necessary to distinguish between them.

Firstly, cryptocurrencies have their own blockchains, whereas tokens are built on an existing blockchain (Ethereum, Waves, etc.). A token is a mean of payment in a specific blockchain, which is based on the underlying cryptocurrency. A token without a cryptocurrency cannot exist, and a cryptocurrency without a token can. Secondly, unlike cryptocurrencies, the issue of tokens is carried out by a person (individual or legal entity) — the initiator of their issue. As a rule, the issue of tokens occurs during ICO and their issue is limited. Thirdly, the ICO token has a wider range of applications. In addition to being used as a payment unit, they can certify various rights. In practice, they can simultaneously: (a) have purchasing power and perform the function of a means of payment in the ecosystem of a particular project or even outside it (cryptocurrency); (b) perform the role of a financial asset (as a rule, an analogue of a stock, bond, deposit or warrant) and be the object of free purchase/sale on the relevant trading platforms and exchange services; (c) certify the ownership or loan of the investor in a project / enterprise (i.e., perform the role of loans and bonds); (d) certify the rights to purchase a certain amount of services, goods/property (so-called app coins or app tokens); (e) be a form of reward for certain actions, etc.

According to some researchers, "a token personalized by its owner for future use may represent an investment, a share in the capital, a copyright, or a restaurant voucher... any amount and any asset in digital form. A token can represent anything. It can be a value, such as bitcoin, or a title of ownership"[18]. Broadly speaking, tokens can symbolize any property right - absolute or relative; they can act as a representation of any object of law. As it is pointed out in the doctrine[19], they resemble undocumented securities.

The token in its essence represents a legal symbol that certifies the rights to civil rights objects by recording them in a decentralized information system. Blockchain provides the storage and accounting of tokens.

To date, there exist no universal approaches to the consideration and interpretations of the term "token". It is often used in legal and economic literature in different meanings.

[18] W. O'Rorke, *Le status juridique des criptoactifs* (2018), available at *https://blockchainpartner.fr/wp-content/uploads/2018/03/Blockchain-cryptoactifs-et-ICO.pdf*.

[19] See L.A. Novoselova, "*Tokenization" of objects of civil law*, Business and Law, 37-38 (2017), available at *https://www.elibrary.ru/item.asp?id=30755294.*

Various notions of the term "token" is stipulated by diverse types of tokens. It should be noted that at the present time, there is no unified system for classifying tokens. In the legal literature, several classifications of tokens are also proposed depending on the types of functions that they perform.

According to the global classical approach, tokens are divided into investment (Security) Token, Utility Token and Payment tokens (Cryptocurrencies). However, in Russia, the legislator took a fundamentally different path by introducing such concepts as "digital rights", "digital financial assets", "utility digital rights".

It should be noted that the term "digital rights" is borrowed from the American term "digital rights", but this term is used in a completely different meaning. In the USA digital rights are understood as a set of human rights to use a computer, access to the Internet, publication of content in a digital environment, its processing, transmission and other rights of Internet users[20]. Whereas in Russia digital rights represent the legal analogue of the term "token".

According to the Russian approach the concept of "digital rights" means the property rights recorded in electronic (digital), which meet two criteria: (i) they must be explicitly named as digital in the law; (ii) they must be acquired, carried out and alienated on an information platform that "meets the criteria established by law". In other words, the rights secured in electronic form can become "digital" only if they comply with these two main criteria.

Digital rights as objects of civil legal relations appeared on October 1, 2019, due to amendments to Articles 128, 141.1 of the Civil Code of the Russian Federation. Article 128 of the Civil Code of the Russian Federation provides that such an object of civil rights as property rights, in addition to non-cash funds and non-documentary securities, include digital rights. Article 141.1 of the Civil Code of the Russian Federation is devoted to them.

According to clause 1 of Article 141.1. of the Civil Code of the Russian Federation, digital rights are recognized as obligation and other rights named in this capacity in the law, the content and conditions of which are determined in accordance with the rules of the information system that meets the criteria established by law.

[20] See G. Goggin et al., *Digital rights in Australia*, Sydney Law School Research, 18-23 (2017), available at *https://www.researchgate.net/publication/330195909_Digital_Rights_in_Australia*.

The exercise, disposal, including transfer, pledge, encumbrance of digital rights by other means or restriction of the disposal of digital rights is possible only in the information system without contacting a third party.

Thus, digital rights represent objects of civil law and belong to the category of "other property". Despite the legislative consolidation of digital rights among the objects of civil rights, there is a discussion around digital rights as objects of civil rights. Various points of view are expressed.

R.B. Golovkin and O.S. Amosova believe that digital rights are "not a possible behavior of subjects of legal relations, but rather a form of expression of subjective rights reflected in civil legislation and relevant information systems. Therefore... digital rights are a kind of subjective rights expressed in digital form and implemented within the framework of information systems"[21].

V.P. Kamyshansky adheres to the point of view that "digital rights are not a special kind of subjective civil rights, different from real or binding rights. They represent binding and other rights, the content and conditions of which are contained in a special information system"[22].

S.I. Suslova and U.B. Filatova believe that "digitalization of rights does not lead to the emergence of a new type of property rights that exist along with mandatory, corporate, exclusive rights, but to a digital way of fixing them"[23]. A similar conclusion is contained in the articles of L.Y. Vasilevskaya[24]. Thus, according to a number of scholars, digital rights in the form in which they are enshrined in the law do not form a new object of civil rights, but represent a digital form /way of fixing traditional civil rights.

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[21] R.B. Golovkin, O.S. Amosova, *"Digital rights" and "digital law" in the mechanisms of digitalization of the economy and public administration*, 51 Bulletin of the Vladimir Law Institute 165 (2019), available at *https://elibrary.ru/item.asp?id=38246588*.

[22] V.P. Kamyshansky, *Digital Rights in Russian Civil Law,* 1 Power of the Law 15 (2019), available at *https://www.elibrary.ru/item.asp?id=42490448*.

[23] S.I. Suslova, U.B. Filatova, *Objects of civil rights in the conditions of formation of the information space of Russia*, Prologue: Law Journal 11 (2019), available at *https://cyberleninka.ru/article/n/obekty-grazhdanskih-prav-v-usloviyah-formirovaniya-informatsionnogo-prostranstva-rossii*.

[24] L.Y. Vasilevskaya, *Token as a new object of civil rights: problems of legal qualification of digital law*, Actual problems of Russian law, 111–119 (2019), available at *https://cyberleninka.ru/article/n/token-kak-novyy-obekt-grazhdanskih-prav-problemy-yuridicheskoy-kvalifikatsii-tsifrovogo-prava*.

*3.1. Features of digital rights*

The legislator refers digital rights to property rights. Therefore, digital rights have all features of property rights, such as: digital law does not exist by itself, it has the ability to belong to a certain person; with the help of digital law, the property interest of its owner is realized; digital right can be alienated; digital right must have a monetary value.

However, in addition to the features inherent in digital rights as a kind of property rights, digital rights have the following specific features.

1) The main distinguishing feature is the virtuality of a digital asset, which is due to its digital form. The exclusively digital form of the object is associated with the use of a computer. Computers process information in encoded form. The code consists of a finite number of characters (binary code, standard six-bit code of the International Organization for Standardization (ISO), etc.)[25]. Information is usually entered automatically, including by directly reading the original documents, etc. The input information is converted by the input devices into signals and stored in storage devices.

The virtuality of digital assets also determines their immateriality, i.e. their lack of material and corporeal substance. The division of goods that are objects of civil rights into tangible and immaterial, depending on their physical nature, is used in legal science to characterize property goods of an immaterial nature[26].

Such a distinction seems important, because historically, things, i.e. objects of the material world, have prevailed in property turnover. The emergence of an electronic form for a number of traditional objects of civil rights, such as money, securities, and the results of intellectual activity, did not lead to a revolution in law, although it created a number of problems. The legal regulation of such objects was lined up by analogy with the regulation of objects having a similar legal nature and the characteristics of a thing.

However, objects in digital form change the nature of interaction between the participants for the following reasons: 1) digital content cannot be read without using a communication device; 2) computers read and transmit digital content by copying

[25] [2017] UKSC 36, [2017] AC 624. Explanations to the Unified Commodity Nomenclature of Foreign Economic Activity of the Eurasian Economic Union (TN VED EAEU) (Volume IV. Sections XIV - XVI. Groups 71 - 84).

[26] L.V. Sannikova, *Services in Russian civil law*, 97 (2006).

it. In this case, any use of the file entails copying it. Even when such copies are temporary or secondary[27].

In my opinion, the specificity of digital assets and their difference from traditional objects, which can exist both in analog form and in digital (electronic), is that they are not only immaterial in nature, but also do not need to be materialized in the real world for their functioning. This property of digital assets is emphasized when certain types of them are characterized as virtual: virtual currency, virtual property, etc.

2) economic value

The use of digital assets such in the financial sector indicates that these objects have a certain value. The fact that the newly generated token or cryptocurrency may not meet the expectations of investors and turn out to be "soap bubbles" has no legal significance. These objects have at least a potential value.

Thus, digital assets with economic value can be recognized as objects of civil rights. It is the economic value of the object that determines its demand among the participants of the property turnover, and, accordingly, participation in the property turnover. At the same time, it should be emphasized that the value is not the code entry itself, but the right certified by it to the object encrypted in it, including the right to access the code (login, password, crypto wallet, etc.), as well as the right to dispose of a digital asset.

3) fixation of digital rights with the help of individual digital technologies (blockchain / distributed registry / decentralized information system) embodied in cryptoassets.

4) the interaction between the participants in civil legal relations regarding digital rights occurs exclusively within the framework of the information system. For utility digital rights, according to the Law On Investment Platforms, it is an investment platform; for digital financial assets - information system, following the Law on DFA.

To sum up, the following definition of digital rights as objects of civil legal relations can be formulated: they are the property rights to objects existing exclusively in cyberspace that are recorded digitally, by creating a record about them in the information system, provided that the holder of such rights has the technical ability to dispose of them.

[27] V.L. Entin, *Copyright in virtual reality (new opportunities and challenges of the digital age)*, 216 (2017).

*3.2. Types of digital rights*

According to the Law on DFA and the Law on Investment Platforms, digital rights are divided into the following categories: digital financial assets (DFA) and utility digital rights. However, digital rights do not include digital currency (cryptocurrency)

Currently, the legislator names as digital rights the following utility digital rights: 1) the right to demand the transfer of the thing (things); 2) the right to demand the transfer of exclusive rights to the results of intellectual activity and (or) the rights to use the results of intellectual activity; 3) the right to demand the performance of work and (or) the provision of services. (Art. 8 of the Law on Investment Platforms).

In accordance with paragraph 2 of Art. 1 of the Law on DFA, digital financial assets (DFA) are digital rights, including monetary claims, the ability to exercise rights to equity securities, the right to participate in the capital of a non-public joint stock company (JSC), the right to demand the transfer of equity securities, which are provided for by the decision on the issue of digital financial assets in the manner prescribed by law, the release, accounting and circulation of which is possible only by making (changing) entries in the information system based on the distributed register, as well as in other information systems (IS).

I believe that digital rights cannot be limited solely to utility digital rights or digital financial assets. For example, utility digital rights are inherently obligation rights. The fact that they are recorded in the information system does not make them digital.

A) Utility digital rights.

The Law on Investment Platforms regulates a specific type of investment relationship - a relationship in which investment is carried out exclusively through the investment platforms.

According to sub-paragraph 1 of Part 1 of Article 2 of the Law on Investment Platforms, an investment platform is an information system in the Internet information and telecommunications network used to conclude investment contracts with the help of information technologies and technical means of this information system, access to which is provided by the operator of the investment platform.

Based on the above definition, the main task of the investment platform is to ensure the conclusion of investment contracts. The following functions of investment platforms can be distinguished:

- ensuring the conclusion of investment contracts (main functions);

- providing additional service to participants of investment relations (auxiliary functions).

The main functions of the investment platform ensure the implementation of the rights of participants in investment legal relations, as well as legal requirements (in terms of ensuring economic security, etc.).

Acquisition, emergence and alienation of issued utility digital rights under Russian law is possible only on investment platforms. Therefore, in order to use the services of the investment platform, the investor enters into an agreement with the operator of the investment platform on the provision of investment assistance services. Both of these agreements are accession agreements.

It should be noted that the definition of an investment contract appeared in Russian legislation for the first time. The implementation of investment is recognized as the main criterion for classifying a contract as an investment one[28]. However, it applies only to investment contracts concluded through investment platforms. In fact, the legislator has identified a special kind of investment contracts. Such contracts, in addition to the feature of investment activity, include specific methods of concluding and executing the contract. Moreover, the method of investment used by the participants determines the terms of the relevant investment agreement.

Thus, the main features of investment agreements are: (i) making investments through the investment platform; (ii) making investments in specific ways that are provided for by Federal Law.

The parties to investment agreements, as well as their place in the system of investment relations, are shown in the following table.

[28] V.N. Lisitsa, *The legal regulation of investment relations: Theory, legislation and practice of enforcement*: Monograph; Russian Academy of Sciences, Institute of Philosophy and Law SB RAS; Ministry of Education and Science of the Russian Federation, Novosibirsk State University. Novosibirsk, 467 (2011), available at *https://www.elibrary.ru/item.asp?id=26096166*.

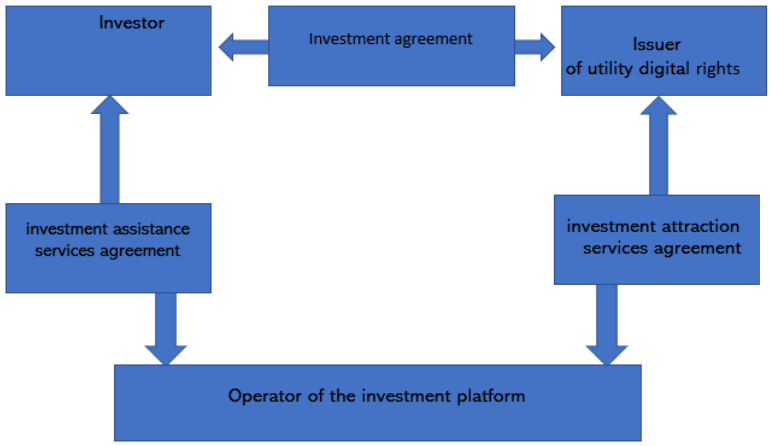


Table 1. System of the investment relations.

A mandatory feature of the parties to the investment agreement is that they must be registered on the investment platform itself as a user (the necessary functions must be available to them in accordance with the rules of such an information system).

1) The operators of the investment platform are an obligatory party to contracts concluded in the process of organizing investment attraction. Only the operators of the investment platform have the right to organize investment attraction. The operator of the investment platform can only be a business company established in accordance with the legislation of the Russian Federation. The activity of the operator of the investment platform can only be carried out by an organization included in the specialized register of the Bank of Russia - the register of operators of investment platforms.

Moreover, investment attraction services can only be provided to persons who meet the established requirements.

Therefore, the operator of the investment platform has the right to conclude the above-mentioned contracts only with persons who meet such requirements, which imposes on him the obligation to establish compliance with the requirements of the legislation of a potential investor or a person attracting investments.

2) An investor can be a natural person or a legal entity. At the same time, the legislation establishes a number of restrictions for attracting investments and investing by individuals.

Thus, the amount of investments that one person can attract during one calendar year should not exceed 1 billion rubles (the restriction does not apply to public joint-stock companies that attract investments by acquiring utility digital rights by investors). Monitoring of compliance with this restriction is carried out by the operator of the investment platform each time a person attracts investments using the investment platform of this operator.

Investing by natural person requires the compliance with special rules and restrictions. A natural person can invest using investment platforms in total no more than 600 thousand rubles during one calendar year. Moreover, this restriction applies to investing in all investment platforms, and not just one. If the total investment volume of an individual exceeds the specified limit, the operators of investment platforms are not entitled to provide an opportunity for a natural person to invest.

This restriction does not apply:

1) to natural person who are individual entrepreneurs and (or) individuals recognized by the operator of the investment platform as qualified investors in accordance with Article 51.2 of Federal Law No. 39-FZ of April 22, 1996 "On the Securities Market";

2) to natural person when they acquire utility digital rights under investment agreements concluded with a public joint stock company.

For each investment by a natural person, the operator of the investment platform is obliged to monitor compliance with this restriction. Such control is carried out by the operator of the investment platform on the basis of the assurances of a natural person on compliance with the specified restriction, submitted in accordance with the procedure provided for by the rules of the investment platform. In case of exceeding the specified limit of the investment amounts of a natural person, the operator of this investment platform may be obliged, at the request of such a natural person, to acquire from him property rights, securities and

(or) utility digital rights acquired in this investment platform for the amount of such excess (the consequence of investing in violation of the established restrictions). A claim for the application of this effect may be filed by the investor within one year from the date of the transaction with exceeding the limit. However, if a natural person has given the operator of the investment platform false assurances about compliance with the restriction, he is deprived of the right to demand that the operator of the investment platform purchase the specified rights, securities from him.

3) An issuer of utility digital rights can be a natural person or a legal entity. The Law on Investment Platforms imposes several requirements on them.

Thus, the issuer of utility digital rights cannot be a natural person who, and (or) whose controlling persons, and (or) the head (sole executive body) of which:

a) included in the list of organizations and individuals in respect of which there is information about their involvement in extremist activities or terrorism, and (or) in the list of organizations and individuals in respect of which there is information about their involvement in the proliferation of weapons of mass destruction;

b) do not meet the requirements established by the rules of the investment platform.

A legal entity cannot be an issuer of utility digital rights if:

a) the controlling persons of such a legal entity and (or) its head (sole executive body) have an outstanding or outstanding criminal record for a crime in the field of economics or a crime against state power, the interests of public service and service in local self-government bodies;

b) in respect of the head (sole executive body) of such a legal entity, the period during which he is considered to have been subjected to administrative punishment in the form of disqualification has not expired;

c) proceedings on bankruptcy of a legal entity have been initiated against such a legal entity.

An individual entrepreneur cannot be a person attracting investments if:

a) has an outstanding or outstanding criminal record for a crime in the field of economics or a crime against state power, the interests of public service and service in local self-government bodies;

b) the arbitration court has introduced the procedure applied in the case of insolvency (bankruptcy) in respect of such an individual entrepreneur;

c) in respect of such an individual entrepreneur, from the date of completion of the procedure for the sale of property or termination of bankruptcy proceedings during such a procedure, the period provided for by Federal Law No. 127-FZ of October 26, 2002 "ON Insolvency (Bankruptcy)" has not expired, during which he is not entitled to carry out entrepreneurial activities, as well as hold positions in the management bodies of a legal entity and otherwise participate in the management of a legal entity.

As part of the investment attraction activity, a person places an investment offer in which, in addition to all the essential terms of the investment agreement, the following must be specified:

- the validity period of such an investment offer;
- the minimum amount of investors' funds, the achievement of which is a prerequisite for the conclusion of an investment agreement;
- the maximum amount of investors' funds, upon reaching which the validity of such an investment offer is terminated (the maximum amount of investors' funds is considered reached if investors accept an investment offer for an amount of funds equal to the specified maximum amount of funds).

As a general rule, the conclusion of an investment contract is confirmed by an extract from the register of contracts issued by the operator of the investment platform. The conclusion of contracts under which utility digital rights are acquired is allowed by confirming information in the register of contracts (if such information is entered into the register of contracts according to the rules for entering information about the emergence of utility digital rights in the investment platform).

B) Digital financial assets

The Law on DFA establishes that the release, accounting and circulation of DFA is possible only by adding entries to an information system based on a distributed registry, as well as to other systems.

According to the legislation, the release, accounting and circulation of DFA are possible only by making (changing) entries in the information system based on the distributed register, as well as in other information systems. This approach seems to be

justified, because, on the one hand, it brings certainty to the understanding of the essence of digital financial assets as a type of cryptoassets, on the other hand, it makes it possible to extend this regulation to similar objects that can be created in the future using other digital technologies. Digital financial assets are accounted for in the information system in which they are issued, in the form of records in the ways established by the rules of the specified information system.

Parties in the system of DFA relations, are shown in the following table.

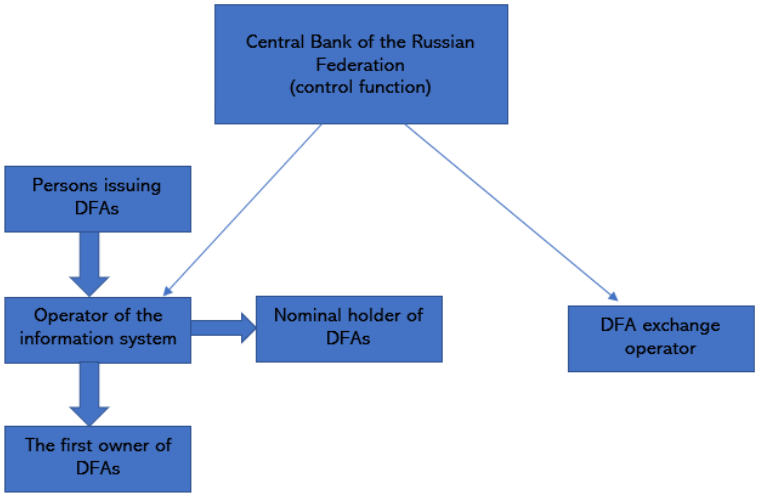


Table 2. System of DFA relations.

The information system may be a legal entity, whose personal law is Russian law (including a credit institution, a person entitled to carry out depository activities, a person entitled to carry out the activities of a trade organizer).

The operator of the information system is obliged to ensure:

1) the ability to restore access of the owner of digital financial assets to the records of the information system at the request of the owner of digital financial assets;

2) uninterrupted and uninterrupted functioning of the information system, including the presence and proper functioning of duplicate (backup) technological and operational means, ensuring the uninterrupted and continuous operation of the information system;

3) the integrity and reliability of information about digital financial assets contained in the records of the information system;

4) the correctness of the implementation in the information system of the algorithm (algorithms) established by the operator of the information system for creating, storing and updating information contained in the distributed register, and the algorithm (algorithms) that ensure the identity of the specified information in all databases that make up the distributed register, as well as the impossibility of entering changes in the algorithm (algorithms) established by the operator of the information system by other persons - for information systems based on a distributed register.

Sale and purchase transactions and other transactions related to DFA are made through the digital financial asset exchange operator, which ensures the conclusion of transactions with the digital asset by collecting and comparing multidirectional applications for such transactions or by participating at its own expense in the transaction with DFA as a party to such a transaction in the interests of third parties.

The status of this entity can be compared to a broker or dealer in the securities market.

The operator of the exchange of digital financial assets can be credit organizations, trade organizers, as well as other legal entities that meet the requirements of this Federal Law and the Bank of Russia regulations adopted in accordance with it, which are included by the Bank of Russia on the basis of their petition in the order established by it in the register of operators exchange of digital financial assets. The operator of the exchange of digital financial assets has the right to carry out its activities from the moment it is included in the register of operators of the exchange of digital financial assets, which is maintained by the Bank of Russia in accordance with the procedure established by it. The register of operators for the exchange of digital financial assets is posted on

the official website of the Bank of Russia in the information and telecommunications network "Internet".

Actions for entering into the information system in which the issue of digital financial assets is carried out, records of the transfer of digital financial assets to their first owner are entitled to carry out Persons issuing DFAs. The law establishes the following requirements to them:

1) individuals registered in accordance with Federal Law No. 129-FZ of August 8, 2001 "On State Registration of Legal Entities and Individual Entrepreneurs" as individual entrepreneurs;

2) legal entities (commercial and non-commercial organizations).

The rights certified by the DFA arise from their first owner from the moment the records of the transfer of digital financial assets to the specified person are entered into the information system in which the DFA is issued.

The owner of digital financial assets is a person who simultaneously meets the following criteria:

1) a person is included in the register of users of an information system in which digital financial assets are taken into account;

2) a person has access to an information system in which digital financial assets are accounted for by possessing a unique code necessary for such access, which allows him to receive information about digital financial assets that he possesses, as well as to dispose of these digital financial assets through the use of an information system.

Digital financial assets can be also credited to a nominal holder of digital financial assets. He keeps account the rights to digital financial assets owned by other persons. Only a person who has a license to carry out depository activities can act as a nominee holder of digital financial assets. The operator of the information system in which the digital financial assets are issued cannot act as a nominal holder of digital financial assets.

The law on the DFA provides that the Bank of Russia is the regulator and controller of the circulation of digital financial assets. However, nowadays there are no standards and rules for protecting the rights and interests of recipients of digital financial services in the new digital market.

To sum up, the Russian legislation establishes the basics of the mechanism of interaction of participants in legal relations on

investing using an investment platform and circulation of financial digital assets through information system, defines legal status of participants and the procedure for concluding transactions with the help of such platform.

It should to be noted that the new concepts introduced by Russian legislators do not correspond to the notions formed in international practice. The use of such terms as "digital rights", "digital financial assets", "utility digital rights" has the following disadvantages.

a) Unlike the global approach, cryptocurrencies and tokens are united by the common concept of "digital financial assets".

b) The term "digital financial assets" is not used in world practice when regulating the crypto market. Accordingly, such terminology will not be clear to foreign investors.

c) The concept of utility rights is revealed in the law by listing digital rights that can be acquired, alienated and implemented in the investment platform. These include: 1) the right to demand the transfer of a thing(s); 2) the right to demand the transfer of exclusive rights to the results of intellectual activity and (or) the rights to use the results of intellectual activity; 3) the right to demand the performance of works and (or) the provision of services. Based on the content of utility digital law, it can be assumed that we are talking about security tokens rather than utility tokens.

Besides, the requirement of only limited range of participants reflects the national character of the Russian legislation on crypto assets. In other words, only Russian legal entities can be operators of the information system and the exchange operators of digital financial assets. In the case of utility digital rights and DFA, the legislator "binds" cross-border relations on the turnover of digital rights to the Russian jurisdiction. This leads to limitation of the number of foreign participants to take part in these relations, as well as intermediary institutions through which all transactions with digital rights must pass. On the one hand, such a system makes it possible to strengthen control over the digital rights market, provide clear rules of participation for ordinary investors and increase general confidence in the new market (in particular, this is facilitated by the introduction of the responsibility of the operator of the information system). On the other hand, it creates an additional obstacle for foreign ICO companies that will have to

comply with new legislative requirements of the Russian Federation (for example, the requirement that persons attracting investments through investment platforms have to be Russian legal entities).

**4. Applicable law**

One of the major problems when it comes to regulating crypto assets is that it goes beyond jurisdiction. Therefore, the fundamental issue in the conflict of laws is whether the territorial, citizenship or domicile theory is the correct basic principle for determining jurisdiction. One of the inherent difficulties of applicability of these principles is stipulated by the anonymous and decentralised nature of blockchain. It is likely that legislation will be required to resolve these issues, potentially requiring international cooperation across jurisdictions. In this regard it is interesting to analyze Russian approach to the law applicable to crypto assets which could help in elaborating the uniform international view.

According to paragraph 5 of Article 1 of the Law on DFA, Russian law applies to legal relations arising during the issuance, accounting and circulation of digital financial assets, including relations with the participation of foreign persons. Thus, Russian law will apply to the legal relations of a foreign investor and a Russian company offering to sell DFA on the territory of the Russian Federation, since the issue of DFA on the territory of the Russian Federation is regulated by the Law.

It has to be noted that although the Law does not directly indicate the law applicable to the purchase of tokens from foreign ICO projects, most likely, the legislator implied that all legal relations arising from transactions with the DFA, in which a person from the territory of the Russian Federation participates, will be regulated by Russian law. This is evidenced by the fact that, according to the Law, it is possible to make a transaction related to the DFA only through the DFA exchange operator. Accordingly, all types of such transactions are covered by Law and Russian law applies to them.

It can be concluded that a citizen of the Russian Federation who is abroad can purchase a DFA in a foreign jurisdiction according to the rules of the country of his location. However, in

Russia, the acquired DFA can be sold only through the DFA exchange operator, whose activities are regulated by Russian law.

In this regard, the DFA exchange operator will act as a kind of intermediary between the resident of the Russian Federation and the person issuing the DFA abroad. In particular, Article 10 of the Law on DFA indicates that the exchange operator can ensure the execution of such transactions in two ways: "by collecting and comparing multidirectional orders for such transactions or by participating at its own expense in a transaction with digital financial assets as a party to such a transaction in the interests of third parties". In other words, if in a foreign jurisdiction an asset token was issued, for example, on the Waves blockchain platform[29], then in Russia the DFA exchange operator can provide a service to residents of the Russian Federation for its acquisition. In this case, on the Waves blockchain platform, the acquirer of such an asset will be the exchange operator of the DFA, and in the information system operated by our intermediary, the owner of such an asset will be a resident of the Russian Federation.

Thus, there are three parties in the legal relationship for the acquisition of a digital asset by a resident of the Russian Federation: an investor, an operator who provides the service "to participate in a transaction with digital financial assets as a party to such a transaction in the interests of third parties", and a foreign entity issuing DFA[30].

The described system of choosing the applicable law is very close to the concept of the Proper Law, namely the law of the state with which this legal relationship is most closely connected. In my opinion, the emergence of operators of information systems, DFA exchange operators, which are Russian legal entities, brings legal relations of DFA closer to Russian law, makes them more closely connected.

As opposed to the Law on DFA, the Law on Investment Platforms does not provide for any provisions on the applicable law. Due to the fact that three parties are involved in the process of circulation of utility digital rights and 3 different contracts are used, it seems appropriate to consider each contract separately.

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[29] Waves Enterprise blockchain platform, available at *https://wavesenterprise.com/ru/platform*.

[30] M.Yu. Kuzmenkov, *Conflict Regulation in Digital Rights Circulation*, 16 Actual Problems of Russian Law, 152 (2021) (In Russ.), available at *https://doi.org/10.17803/10.17803/1994-1471.2021.124.3.152-159*.

The question of applicable law arises only when the legal relationship involves a foreign element. In the doctrine of private international law, the foreign element is usually expressed in the subject of legal relations, the object of legal relations and a legal fact[31]. A legal fact (the acquisition of utility digital rights) takes place on the territory of the Russian Federation, since according to the Law, "digital rights arise from the first acquirer, passes from one person to another person and (or) terminates from the moment information about this is entered in the investment platform". The object of legal relations is digital law, which actually exists in the form of a computer code. Undoubtedly, it can technically be located on foreign servers. However, given the absence of a significant legal connection between the location of such digital rights and the actual legal relationship of the parties, as well as the difficulty of locating in the case of using a distributed data registry, the object of legal relationship should not be regarded as a foreign element that influences the choice of applicable law. As for the subjects of legal relations, there are three of them: the operator of the investment platform, the investor and the issuer of utility digital rights.

According to the Law on Investment Platforms, an investment platform operator is always a Russian legal entity. Accordingly, it cannot be a foreign element. The law also indicates that the issuer of utility digital rights) is "a legal entity created in accordance with the legislation of the Russian Federation, or an individual entrepreneur to whom the investment platform operator provides investment attraction services". Consequently, the issuer of such digital rights is also a person whose personal law is Russian law. But the Law refers to an individual or legal entity as an investor without reference to Russian law. Such a person may be a foreign citizen, who will be the only possible foreign element in these legal relations. As already noted, the investor enters into an investment agreement with the issuer of utility digital rights using the technical means of the investment platform. It was also noted that the register of investment agreements is maintained by the operator of the investment platform, the conclusion of agreements takes place on the investment platform, the issue and circulation of utility digital rights also occur within the investment platform. Both the operator

[31] I.B. Ilovaisky, *On the definition of "foreign element" in private international law and ease of understanding of law*, Legal Concept, 99–106 (2019), available at *https://cyberleninka.ru/article/n/o-definitsii-inostrannyy-element-v-mezhdunarodnom-chastnom-prave-i-prostote-ponimaniya-prava*.

of the investment platform and the issuer of utilitarian digital rights are residents of the Russian Federation. Based on this, it can be concluded that these legal relations are most closely related to Russian law, which is to be applied.

However, the application of Russian law to such relations is fair only from the Russian legislation perspective. In other countries, there may be other conflict-of-laws rules to legal relations arising from the issuance and turnover of DFA. Besides, in most countries, there are no special laws that regulate the turnover of utility digital rights, known abroad as utility tokens. Such tokens by their nature are usually compared with the product[32]. In this regard, Regulation (EC) N 593/2008 on the law to be applied to contractual obligations (Regulation "Rome I")[33]. This Regulation applies in situations containing a conflict of laws to contractual obligations in the civil and commercial area. Thus, the Regulation establishes that the contract of sale of goods is governed by the law of the country where the seller has his usual place of residence, and the service contract is governed by the law of the country where the service provider has his usual place of residence. Therefore, if in law enforcement practice there is a situation of recognizing a utility token as a product or service, there is the possibility of using conflict-of-laws bindings established in the Rome I Regulations. The key point is to determine the legal nature of the token in a particular jurisdiction in order to understand whether we can apply certain conflict-of-laws rules.

## 5. Conclusion

Due to the global nature of ICOs, the elaboration of its global regulation could become quite an extensive exercise, in which an assessment of the experience of other jurisdictions could be very useful. Thus, the choice to analyze Russian ICO framework was natural due to its recently passed federal laws in this area.

Assessing in general the Russian legislation in the field of crypto assets, it should be recognized that Russia has not managed

[32] Legal Classification of Tokens: Utility Token, available at *https://www.lexology.com/library/detail.aspx?g=c1d69ffb-c010-4ffe-8923-841a804907db*.

[33] Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations, OJ L 177, 4.7.2008, p. 6, SPS "Garant".

to avoid conceptual miscalculations and inconsistencies in creating its own model of legal regulation, which lead to difficulties in its practical implementation.

Firstly, the exclusively national character of the adopted Russian legislation needs to be stressed. In particular, this is manifested in the rejection of terminology that has accepted worldwide and introducing such concepts as "digital rights", "digital financial assets", "utility digital rights". Meanwhile, the name of various types of crypto assets is of great importance for the formation of supranational legislation. Such requirements and the general difference from the legal practices of regulating the turnover of digital rights in the vast majority of jurisdictions can significantly reduce the desire of foreign ICO projects to enter the Russian market. It is unlikely that this will contribute to the formation of the image of the Russian jurisdiction as friendly and open for the introduction of new digital technologies and for investments in this area. Therefore, it seems appropriate to harmonize national legislation with the world practice of turnover of crypto assets. Reverse approach can negatively affect the investment attractiveness of the Russian digital asset market.

Secondly, in Russia exist no special rules to protect consumers and provide them with special rights as compared with professional investors (e.g. for disputes).

Thirdly, there is no special state supervisory authority for this area of relations. The Bank of Russia collects information from citizens about unscrupulous financial companies, including those that hide behind crypto-legends. For this purpose, a special department for countering unfair practices in the financial market has been established. But the Bank of Russia does not have any opportunities to influence the alleged fraudsters if they do not have permits (licenses) issued by the regulator itself. His task in this case is to collect, summarize information and transfer it to law enforcement agencies for investigation.

Fourthly, the size of the territory of Russia predetermines the large distances between the centers of economic activity, the presence of remote territories in the constituent entities of the federation, which generates significant inequality. In other words, at the federal level, the legislator adopts general framework laws that establish the principles and main directions of regulation and regional legislation establishes the specification of federal normative legal acts, taking into account the local specifics and

features of the formation of local self-government in the subjects of Russia.

All in all, the example of the Russian ICO laws illustrates some of the obstacles that may be encountered when trying to elaborate global and uniform approach towards ICO regulation. Identifying these difficulties at an early stage will help to avoid possible future mistakes.

Therefore, on the global level the legislators should take into account the following recommendations while elaborating the uniform ICO regime. In particular, regulators should not introduce fundamentally new concepts and categories, but tend to harmonize the conceptual framework as much as possible. Moreover, it seems necessary to set rules in order to protect consumers and provide them with special rights as compared with professional investors (e.g. for disputes). In addition, it is recommended to form the new global organization that would present a comity with the representatives of States national authorities. Members of such organisation would cooperate closely and having this kind of interaction as everyday practice makes easier to prove facts that cannot be changed without a trace. The ultimate goal of this organization should be the development of best practice standards and common global ICO framework.