

**BITCOIN IN CHINA:  
A LEGAL PERSPECTIVE**

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## Background

On November 1, 2008, an academic paper describing a new digital currency was published by Satoshi Nakamoto (a pseudonymous person or group of people) in *The Cryptography Mailing List* at metzdowd.com, where the term “Bitcoin” was born. In 2009, Nakamoto released the first software that launched the Bitcoin network. The first units of the currency and subsequent first deal were made afterwards.

In 2012, one Bitcoin was worth between USD 12-13. By October 2013, one Bitcoin reached USD 205. As Bitcoin began to gain ground, speculators appeared, contributing to the price of Bitcoin breaking the USD 1,000 mark. As Bitcoin has proliferated, transactions made with it have included items from candy sales to tuition payments, as well as illegal drug and gun deals.

The value of Bitcoin shows a broadening acceptance of its holders and potential holders, as well as recognition from government bodies. “The German Ministry of Finance classifies bitcoins not as e-money or a functional currency, but something to be subsumed under the German term of ‘Rechnungseinheit’ as a financial instrument,” Martin Chaudhuri of Germany’s Ministry of Finance was quoted as saying in August of 2013.

While Bitcoin becomes more widely known, the virtual currency has potential risks that cannot be ignored. U.S. comedian Stephen Colbert has joked that “Bitcoin has worth just because a bunch of people on the Internet have agreed it is worth something -- like Psy”. The former president of the Dutch Central Bank, Nout Wellink, has compared the hype and speculation about Bitcoin to his country’s 17th century “tulip mania”, a period in the Dutch Golden Age when prices for the flower reached unforeseen high levels and then suddenly fell. In other words, Bitcoin differs from common currencies as there isn’t anything of any fundamental value backing it up. What makes the situation even more peculiar is that there is no legal authority responsible for the currency’s relevant legal liabilities. As Wellink stated during a talk at the University of Amsterdam in May of 2013: “This is worse than the tulip mania...at least then you got a tulip [at the end], now you get nothing.”

## Bitcoin in China

Nearly 1.8 million Bitcoins were traded on the BTC China trading platform in November 2013 alone, making it the platform with the highest trading volume in the world, according to *Bitcoincharts*, which monitors data related to the Bitcoin network. As China now boasts the highest demand for Bitcoins, a “*Bitcoin Risk Prevention Notice*” (Yin Fa [2013] No. 289) was jointly released by the People’s Bank of China, Ministry of Industry and Information Technology, China Banking Regulatory Commission, China Insurance Regulatory Commission, and China Security Regulatory Commission on December 5 of this year.



The notice first identifies Bitcoin's nature: it is not issued by a competent authority, does not share currency characteristics such as enforcement and statutory tendering, and is therefore not a true currency.

Second, the notice clarifies that neither financial nor payment institutions are allowed to do the following:

- Price Bitcoin as a product or service
- Use Bitcoin in dealing with the central government
- Engage in insurance services that have connections with Bitcoin
- Bring Bitcoin into the scope of subjects of insurance
- Either directly or indirectly provide services relevant to Bitcoin to customers (including providing services such as registration, liquidation, settlement of Bitcoins to customers)
- Accept or use Bitcoin as a payment instrument
- Operate currency exchanges between Bitcoin and Renminbi/other foreign currencies
- Store, host and mortgage Bitcoin
- Issue financial products connected with Bitcoin
- Set up trusts or other funds for Bitcoin investments

Third, the notice stipulates that, subject to the "Telecommunication Regulations of the People's Republic of China", and "the Administrative Measures on Internet Information Services", internet websites providing Bitcoin registration and transactions shall be recorded by the telecommunications administrative authority. The telecommunications authority may shut down Internet websites that unlawfully conduct Bitcoin activities, according to China's laws and regulations.

Regarding the legal risks underlying Bitcoin transactions, and the effects brought with it, we have come to the following conclusions:

Bitcoin was born as a normal electronic virtual merchant, which is not allowed to be utilized as either a currency that can be freely used, or as a foreign currency. Bitcoin differs from traditional articles, with no intrinsic value and being produced through network node calculation. Anyone is able to produce Bitcoins, although the number of Bitcoins will be limited to 21 million according to the current format. It cannot be denied that private citizens are allowed to spend Bitcoins on items agreed to for a certain price, domestically or in other countries.

The government notice breaks the chain connecting Bitcoin and the financial system in order to prevent any financial and legal risks. However, as far as the enterprises and individuals that are not defined in the notice are concerned, these parties are allowed to engage in Bitcoin transactions (subject to the notice and China's regulations). Both parties, however, must deal with any transaction issues that arise out of any deals.

In addition, the last part of the notice states "each of the finance regulatory bodies may, in accordance with this notice, enact relevant implementation rules." With respect to the relevant bodies only enacting implementation rules within the framework of the notice, the rules are only as tight as the notice itself.

We presume that recent government announcements from the Chinese government as well as the governments of other countries regarding Bitcoin should not be considered isolated incidents, as there is a fundamental risk with Bitcoin exchanges. The recent announcements regarding Bitcoin from China as well as other countries should not be considered isolated incidents, as fundamental risks are inevitable during Bitcoin exchanges. There is also the speculation risk that the price of Bitcoin will drop when earlier investors sell considerable amounts of Bitcoin in order to cash them in. The risks involved with Bitcoin were taken into account when China set up regulatory rules.

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