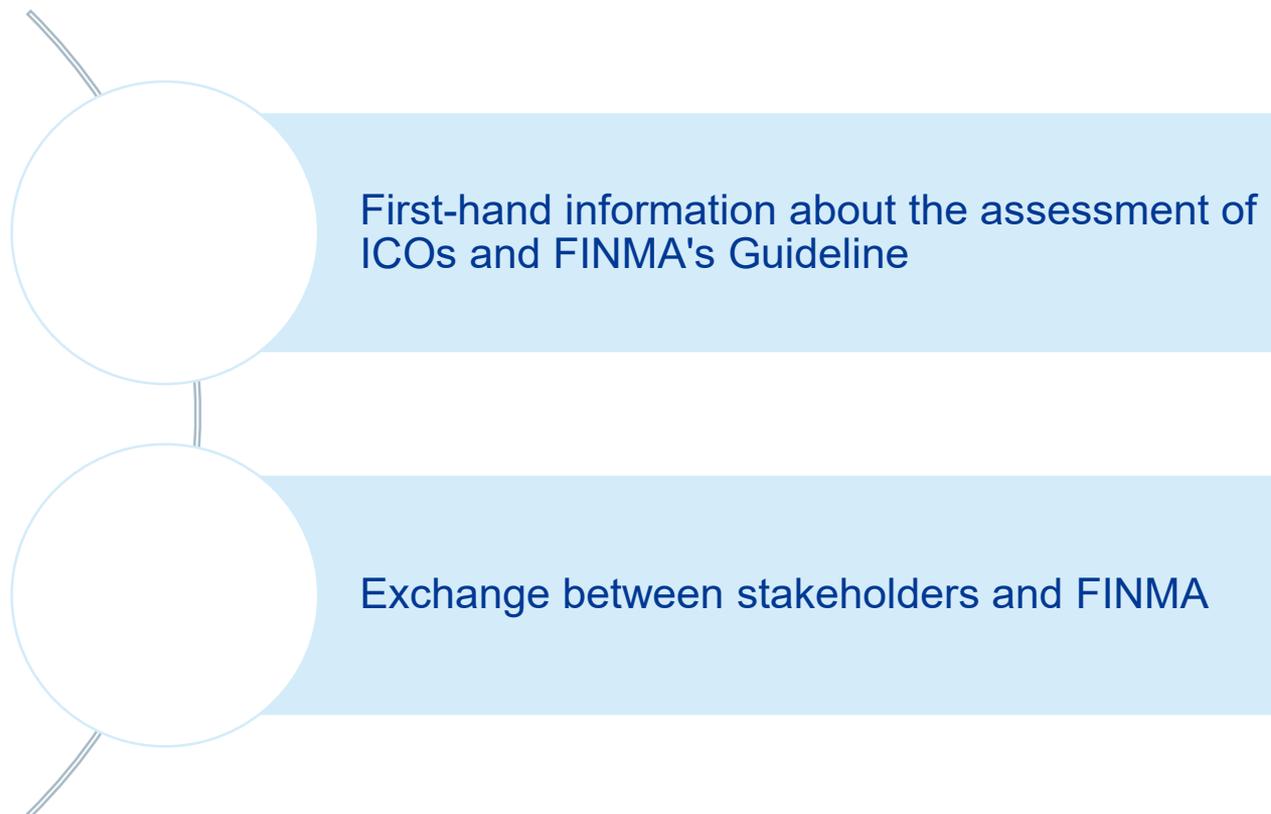


FINMA Roundtable on ICOs

March 2018

Aim of today's roundtable



Agenda

- Introduction
- Regulatory and supervisory framework for ICOs
- Going forward
- Q & A



Introduction

FINMA's role as a financial market supervisory authority



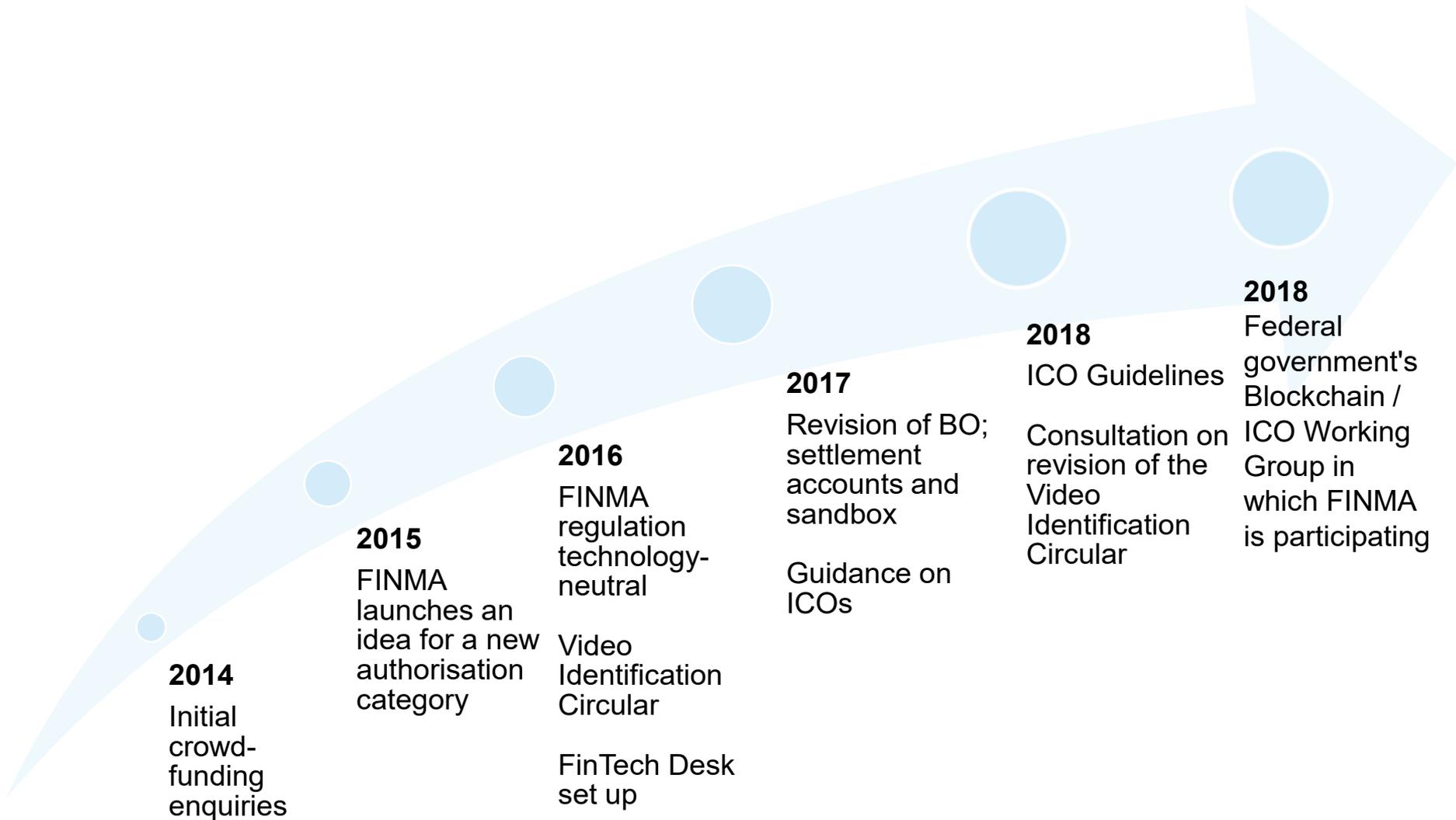
FINMA welcomes innovation under strategic goals 2017-2020

Goal 5:

FINMA will push for the removal of unnecessary regulatory obstacles for innovative business models.

- No unnecessary obstacles to innovative business models
- Principle-based, technology-neutral and competition-neutral regulation and supervision
- Transparency and legal clarity
- Zero tolerance of criminal behaviour

FINMA and FinTech developments





Regulatory and supervisory framework for ICOs

Token categories

- **Payment tokens:** (cryptocurrencies) give rise to *no claims on their issuer*. They are *intended to be used*, now or in the future, as a *means of payment* for acquiring goods or services or as a *means of money or value transfer*.
- **Asset tokens:** represent *assets* such as a debt, equity or other *claim on the issuer*, e.g. a share in future company earnings or capital flows. In terms of their economic function, these tokens are analogous to equities, bonds or derivatives. Tokens which enable physical assets to be traded on the blockchain also fall into this category.
- **Utility tokens:** *provide access* digitally to an *application or service* by means of a blockchain-based infrastructure *at the point of issue*.
- The function of a token and, as a result, its classification may change over time.
- Individual token classifications are not mutually exclusive. Asset and utility tokens can also be classified as payment tokens (referred to as hybrid tokens). In these cases, the requirements are cumulative; in other words, the tokens are deemed to be both securities and a means of payment.

Tokens under securities law – asset tokens

Securities regulation is intended to ensure that market participants can base their *decisions regarding investments* such as equities or bonds on a reliable and defined set of information. Moreover, trading should be fair, reliable and offer efficient price formation.

Securities ("*Effekten*") are defined as: standardised certificated ("*Wertpapiere*") and uncertificated securities ("*Wertrechte*"), derivatives and intermediated securities ("*Bucheffekten*"), which are suitable for mass trading. (Art. 2 let. B FMIA [FinfraG])

Securities suitable for mass standardised trading encompass certificated and uncertificated securities, derivatives, and intermediated securities which are *publicly offered for sale in the same structure and denomination or are placed with more than 20 clients, insofar as they have not been created especially for individual counterparties*. (Art. 2 para. 1 FMIO [FinfraV])

Tokens under securities law – asset tokens

Uncertificated securities are *rights* which, based on a *common legal basis* (articles of association/issuance conditions), are issued or established *in large numbers* and are *generically identical*. Any fungible claim or membership right (*vertretbares Forderungs- oder Mitgliedschaftsrecht*) can be the basis of uncertificated securities (*Wertrechte*). This includes, but is not limited to, tokenised debt or equity instruments such as shares or debentures.

The only formal requirement to create uncertificated securities is to keep a ledger in which details of the number and denomination of the uncertificated securities issued and of the creditors are recorded (*Wertrechtbuch*, Art. 973c para.3 CO [OR]). There are no requirements as to the form of the uncertificated securities ledger. It can be kept on a blockchain.

The issuance (distribution) of tokens is not a prerequisite for the creation of uncertificated securities. In the case of the *pre-financing* and *pre-sale* phases of an ICO which confer claims to acquire tokens in the future, these claims will also be treated as securities if they are standardised and suitable for mass standardised trading.

Tokens under securities law – payment tokens

There are various legal opinions as to whether tokens which give rise to no claims on their issuer (in particular *payment tokens*) constitute securities.

Given that payment tokens are designed to act as a means of payment (i.e. for the purpose of acquiring goods or services or as a means of money or value transfer) and are not analogous in their function to traditional securities, FINMA will not treat payment tokens as securities.

If payment tokens were to be classified as securities through new case law or legislation, FINMA would accordingly revise its practice.

Tokens under securities law – utility tokens

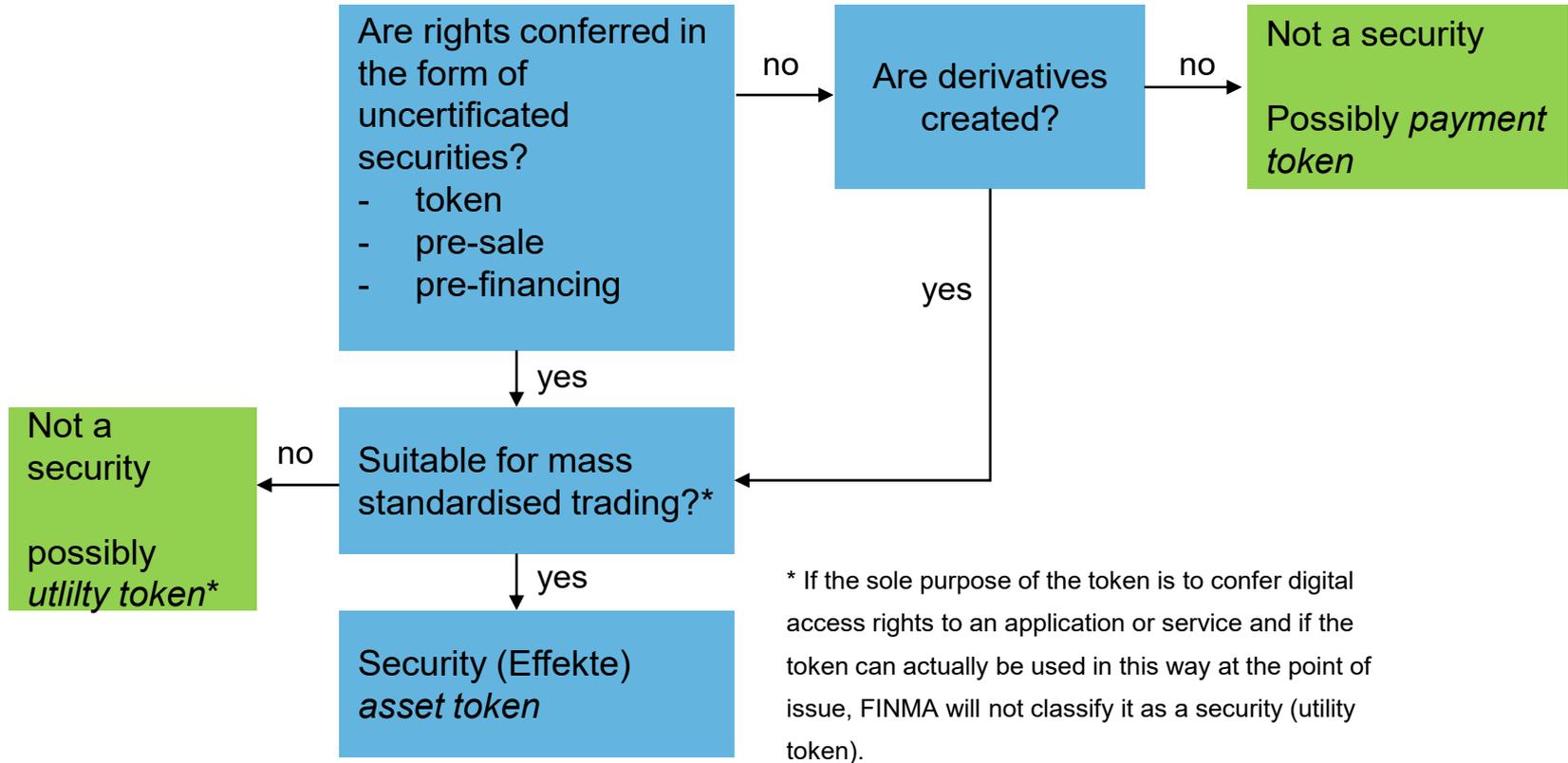
Utility tokens are intended to provide access digitally to an application or service by means of a blockchain-based infrastructure.

In order to qualify as a utility token according to the FINMA guidance, the following requirements must be met:

- The sole purpose of the token is to confer digital access rights to an application or service (i.e. *no investment function*) and
- a token can actually be used in this way *at the point of issue*.

In such cases, where the connection with capital markets, which is a typical feature of securities, is missing, FINMA will not classify tokens as securities.

Tokens under securities law - overview



* If the sole purpose of the token is to confer digital access rights to an application or service and if the token can actually be used in this way at the point of issue, FINMA will not classify it as a security (utility token).

Applicability of securities law – implications I

Implications for ICO organisers:

- Self-issuance of securities is not regulated under FMIA [FinfraG] or SESTA [BEHG]. The same applies to the public offering of securities to third parties without intermediaries.
- However, the creation and issuance of derivative products as defined by FMIA to the public on the primary market is regulated (Art. 3 para. 3 SESTO [BEHV]).
- The issuing of equities or bonds can result in prospectus requirements under the Swiss Code of Obligations, which are currently not subject to supervisory law.

According to the draft Financial Services Act (FinSA), prospectus requirements will become part of supervisory law (Art. 37 Draft FinSA). The Swiss Code of Obligations and FinSA provide for a number of different exceptions and exemptions.

Applicability of securities law – implications II

Implications for intermediaries:

- Underwriting and offering tokens constituting securities of third parties (e.g. an ICO organiser) publicly on the primary market, if conducted in a professional capacity, is a licensed activity (Art. 3 para. 2 SESTO [BEHV]).
- Client dealers, i.e. securities dealers who, in a professional capacity, trade in securities in their own name for the account of clients and maintain accounts for these clients themselves or with third parties for the settlement of transactions or hold securities of these clients in safe custody themselves or with third parties in their own name (Art. 3 para. 5 SESTO [BEHV]), are also subject to FINMA licensing requirements.
- Specific licensing requirements apply for trading venues (stock exchanges or multilateral trading venues, Art. 26 seqq. FMIA [FinfraG]) and organised trading facilities (Art. 42 seqq. FMIA [FinfraG]).

Classification as deposits

- The primary purpose of the Banking Act is to protect the public, particularly bank creditors and their deposits.
- The issuing of tokens is not generally associated with *claims for repayment* on the ICO organiser.
- To this extent, there is no requirement to obtain a banking licence.
- Liabilities with debt capital character (e.g. promises to return capital with a guaranteed return) are treated as deposits.
- Possible exceptions under the Banking Act:
 - Consideration from a contract for the transfer of ownership or for the rendering of a service or transfer as a security (Art. 5 para. 3 let. a BO)
 - Bonds or other debt instruments which are standardised and issued en masse and other uncertificated rights with a similar function (uncertificated securities) (Art. 5 para. 3 let. b BO).

Applicability of the Collective Investment Schemes Act

- The purpose of the Collective Investment Schemes Act is to protect investors and ensure the proper functioning of the market for investment fund products.
- The provisions of the Collective Investment Schemes Act are relevant only if the funds accepted in the context of an ICO are managed by third parties.

Applicability of the Anti-Money Laundering Act

- The objective of the Anti-Money Laundering Act (AMLA) is to protect the financial system from money laundering and the financing of terrorism.
- Anyone who provides payment services or who issues or manages a means of payment is a financial intermediary subject to the AMLA (Art. 2 para. 3 let. b AMLA).
- Definition of a means of payment:
 - Transfer of assets by a third party in the context of a payment system
 - Regardless of whether the payment system can only be accessed by a limited number of users
 - Not subject to AMLA: *two-party relationship* (issuer of the means of payment = user of the payment system).

Issuing of payment tokens

Payment tokens are designed to act as a means of payment



Tokens can be transferred technically on a blockchain infrastructure



Issuing of a means of payment

Issuing of utility tokens (and hybrids with utility element)

- In the case of utility tokens, anti-money laundering regulation is not applicable as long as the main reason for issuing the tokens is to provide access rights to a non-financial application of blockchain technology
- In other words, if the payment function of the utility tokens is an "*accessory service*" (Art. 2 para. 2 let. a no. 3 AMLO) the issuing of such tokens does not constitute the issuing of a means of payment.
- Classification as an "accessory service" (cumulative):
 - Service which is integrated into a contractual relationship unrelated to the financial sector
 - Contracting party which provides the primary service also provides the accessory service
 - The accessory service is of subordinate importance to the primary service.
 - Provision of the primary service is not necessarily possible without the token.

Compliance with AMLA

Due diligence and reporting requirements involve among others:

- not accepting assets originating from criminal activities
- establishing the identity of the client and the beneficial owner(s) of the assets (q.v. Video and online identification circular)
- clarifying the economic background of suspicious business relationships
- clarifying and recording relationships and transactions involving increased risk
- complying with organisational measures
- filing a report with the Money Laundering Reporting Office Switzerland (MROS) where suspicions of money laundering arise.

Affiliate to a self-regulatory organisation (SRO)

- Individuals and companies in the para-banking sector who accept or hold assets on a professional basis or assist in the investment or transfer of such assets must affiliate to a self-regulatory organisation (SRO) or to be subject directly to FINMA supervision.
- These requirements can be fulfilled by having the funds accepted via a financial intermediary who is already subject to AMLA in Switzerland and who meets the due diligence requirements on behalf of the organiser.



→ The ICO organiser does not have to be affiliated to an SRO or licensed directly by FINMA.

Exchange of cryptocurrencies

- Purchase and sale of cryptocurrencies on a commercial basis (cryptocurrency to fiat money / fiat money to cryptocurrency / cryptocurrency to cryptocurrency)
- Offering of services to transfer tokens if the service provider manages the private key (custody wallet provider)

→ Anti-money laundering regulation is applicable.

Summary

Overview:

| | Pre-financing and pre-sale / The token does not yet exist but the claims are tradeable | The token exists |
|-----------------------|---|--|
| ICO of payment tokens | = Securities ≠ subject to AMLA | ≠ Securities = means of payment under AMLA |
| ICO of utility tokens | | ≠ Securities, if exclusively a functioning utility token = Securities, if also or only investment function ≠ means of payment under AMLA, if accessory |
| ICO of asset tokens | | = Securities ≠ means of payment under AMLA |

Going forward – enquiries

- FINMA will respond to enquiries that comply with the minimum information requirements set out in the appendix to its guidelines. To enable FINMA to respond effectively, ICO organisers need to define and document clearly the terms and conditions of their planned ICO as set out in the guidelines.
- ICO enquiries submitted to FINMA **prior** to the publication of the guidelines: FINMA will approach ICO organisers for further clarification where necessary.
- FINMA looks at enquiries solely from the perspective of existing financial market regulation. Market participants themselves remain responsible for complying with other obligations, especially under civil law (such as a potential prospectus requirement).

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