CAREY OLSEN

Jersey publishes ICO guidance note

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The Jersey Financial Services Commission has published its final Guidance Note in relation to Initial Coin Offerings (ICOs). The Guidance Note follows in the wake of several high profile crypto ventures launching from Jersey, including the launch of several ICOs. The Guidance Note formalises the road map for approval previously developed by the JFSC in consultation with Carey Olsen who have advised on all Jersey ICOs to date.

The Guidance Note adopts a pragmatic approach, focusing on consumer protection and anti-money laundering and having regard to the fact that ICO promoters want to use Jersey because of the Island's reputation as a well-regulated and reputable jurisdiction.

In order to give prospective ICO investors a degree of disclosure and comfort that may not be available in many other jurisdictions - and being mindful of the guiding principle pursuant to which the JFSC discharges its functions as the Island's financial services regulator – the JFSC sets out certain requirements on an ICO issuer which are set out below. This briefing note summarises the Guidance Note's principal features - a link to the full Guidance Note can be found here.

JFSC requirements on a Jersey ICO issuer

The ICO issuer is required to:

- be a Jersey company
- receive consent from the JFSC before it undertakes any form of activity (see "Application Process" below")
- comply with the JFSC's Sound Business Practice Policy (see below)
- apply relevant AML/CFT requirements to either purchase tokens from or sell tokens back to the Issuer
- appoint a Jersey licenced administrator
- appoint and maintain a Jersey resident director on the board
- be subject to an ongoing annual audit requirement
- have procedures and processes in place to (i) mitigate and manage the risk of retail investors investing inappropriately in the ICO, and (ii) ensure retail investors understand the risks involved
- prepare an information memorandum which complies with certain content requirements required under Jersey company law
- ensure that any marketing material is clear, fair and not misleading, and include in any such materials certain prescribed consumer warnings

Security v non security tokens

Before the issuer can undertake any activity, it requires a consent from the JFSC under the Island's statutory instrument governing the raising of capital, the Control of Borrowing (Jersey) Order 1958 ("COBO"). The type of COBO consent granted by the JFSC will depend on whether the token is categorised as a "security" under COBO.

While there is no precise definition of what constitutes a "security" under COBO, the Guidance Note stipulates that a token which has one or more of the following characteristics will be regarded by the JFSC as a "security":

- a right to participate in the profits/earnings of the issuer or a related entity

- a claim on the issuer or a related party's assets
- a general commitment from the issuer to redeem tokens in the future
- a right to participate in the operation or management of the issuer or a related party
- expectation of a return on the amount paid for the tokens

Importantly and helpfully, there is an express statement in the Guidance Note that the JFSC will not treat a utility token (i.e. a token conferring a usage right and with no economic or voting rights), as a security token solely by reason of the fact that it might be traded in the secondary market (e.g. listed on the cryptocurrency exchange).

Whether or not a token is a "security" under COBO makes no difference as to the requirements imposed on an issuer by the JFSC.

Application process

Application for the issuer's COBO consent is to be accompanied by analysis prepared by the issuer's legal advisers outlining:

- the proposed activity including relevant timelines
- details of the issuer and the ICO
- rationale for the ICO, amount to be raised and use of proceeds
- a summary of the features of the tokens
- a summary of the token purchase and redemption processes
- the service providers to the issuer
- the relationship between issuer and holder of tokens
- the management of underlying assets and security rights over such assets (if any) for holders of the tokens
- how the activity will be wound up/dissolved and assets (if any) distributed to the holders of the tokens
- a Jersey legal and regulatory analysis, including consideration of relevant legislation or other regulatory laws (for example, whether the ICO is a "collective investment fund" under Jersey law)

Following grant of the COBO consent the issuer must seek the prior consent of the JFSC to any material change to the matters contained in the application.

JFSC's Sound Business Practice Policy

The Guidance Note makes clear that an ICO is a "sensitive activity" under the JFSC's Sound Business Practice Policy. The practical consequence of this is that certain AML/CFT obligations are imposed on the issuer, being an obligation to carry out checks on (i) the purchasers of the tokens who purchase coins directly from the issuer, and ii) the holders of tokens issued by the issuer in the event they are sold back to the issuer. In such circumstances, the issuer will be required to obtain information: to (a) establish and obtain evidence to verify identity, and (b) establish and depending on the level of risk obtain evidence to verify the source of funds and source of wealth.

Ongoing requirements imposed on the issuer

- The JFSC's prior consent is required for any change of Jersey administrator or Jersey resdent director.
- The board of the issuer is required to advise the JFSC promptly if the issuer defaults on any token issued.
- The directors of the issuer are required to make an annual confirmation to the JFSC (at the same time as the normal company annual return) that, to the =best of their knowledge and belief, there have been no breaches of the conditions set out on the issuer's COBO consent

Summary

The JFSC's new Guidance Note sets out a clear, practical path for ICO promoters wanting to launch their ICO from a reputable, well regulated jurisdiction. The Guidance Note strikes a well considered balance between a crypto friendly approach from the regulator with the need for appropriate measures place to ensure proper disclosure and good governance.

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