



**Jersey Financial
Services Commission**

Guidance Note

The Application Process for Issuers of Initial Coin Offerings (ICOs)

Issued: July 2018

1 Background

- 1.1 The use of virtual currencies and tokens (hereafter **tokens**) to facilitate economic transactions, raise capital and provide proof of ownership or rights has risen dramatically recently. Excitement over the potential future applications of distributed ledger technology has grown apace. The abundance of innovation has been equally matched by new risks and vulnerabilities, including: high levels of price volatility, loss of funds through cyber-attacks, lost wallet keys and sending payments to wrong recipients; an alarmingly high number of scam projects; wildly over-hyped projects with no real economic substance; and exchange price manipulation through pump-and-dump schemes and other unethical practices of disproportionately large market participants. There are as many ways to lose money in virtual assets as there are to make money.
- 1.2 ICOs are a digital way of raising funds from the public using distributed ledger technology. The ways in which ICOs are structured vary from technical, functional and business perspectives. There is on-going international discussion about whether tokens should be treated as shares, securities, currencies or commodities or some combination of all of the foregoing for regulatory purposes.
- 1.3 The Jersey Financial Services Commission (**JFSC**) recognises the innovative potential of distributed ledger technology and fintech generally. We note that the government of Jersey also recognises the potential of this technology and, more widely, the development of digital industries and growth of entrepreneurial talent in Jersey. However, investors who participate in ICOs should be aware that such an investment is likely to be highly speculative and that they risk losing their investment. This is of particular concern for retail investors, where the nature of any loss may be more severe and they may find it more difficult to understand the nature of the investment being offered.
- 1.4 Most ICOs are unlikely to be regulated by the JFSC¹. Instead, the JFSC places some conditions on an issuer of an ICO (an **ICO issuer**) through the powers conferred on the JFSC in the Island's statutory instrument governing the raising of capital, the Control of Borrowing (Jersey) Order 1958 (**COBO**). Under COBO, a consent is required from the JFSC to establish a Jersey company (a **COBO Consent**). In granting such COBO consent the JFSC may choose to impose certain conditions on the company to which the COBO Consent is granted. As a general policy, Jersey-based ICO issuers are required to be incorporated as a Jersey company and administered through a trust and company service provider licensed by the JFSC under the Financial Services (Jersey) Law 1998 to carry on trust company business (**TCSP**).
- 1.5 The JFSC has to date been reviewing applications by ICO issuers for COBO Consents on a case-by-case basis. Based on the JFSC's experience, and having consulted with the government of Jersey, we have issued this guidance note to clarify the COBO Consent process that the JFSC expects to adopt for future ICO issuers (the **JFSC ICO Issuer Requirements**). The government of Jersey endorses the approach set out in this note.

¹ There is a potential that the structure of some ICOs may result in the issuer being regulated by the JFSC for conduct, prudential or AML/CFT purposes. This guidance refers only to the treatment of ICOs under the Control of Borrowing (Jersey) Order 1958, and therefore issuers or potential issuers need to consider aspects of the wider legislative framework that may apply.

- 1.6 An ICO issuer will need to comply with the attached JFSC ICO Issuer Requirements. The JFSC has also made an amendment to the Sound Business Practice Policy confirming that Jersey-based ICO issuers need to comply with this guidance and the JFSC ICO Issuer Requirements.
- 1.7 This guidance and the JFSC ICO Issuer Requirements will be reviewed and updated periodically where appropriate.

2 Classification of ICOs in Jersey

- 2.1 In reviewing ICO issuer applications, the JFSC will focus on the economic function and purpose of the tokens to be issued. The key factors are the underlying purpose of the tokens and whether they are tradeable or transferable. At present, there is no universally recognised terminology for the classification of tokens either in Jersey or internationally. However, for the purposes of COBO, tokens issued pursuant to an ICO will be classified as either a "security" or not.
 - 2.1.1 **Security Token:** The definition of "security" in COBO is potentially quite wide ranging. A security token would typically have characteristics usually associated with an equity or debt security in the traditional capital markets sense, including one or more of the following such characteristics (whether contractual or implied):
 - 2.1.1.1 a right to participate in the profits/earnings of the ICO issuer or a related entity,
 - 2.1.1.2 a claim on the issuer or a related party's assets,
 - 2.1.1.3 a general commitment from the ICO issuer to redeem tokens in the future,
 - 2.1.1.4 a right to participate in the operation or management of the ICO issuer or a related party
 - 2.1.1.5 expectation of a return on the amount paid for the tokensFor the avoidance of doubt, a utility token (see below) will not be regarded a "security" solely by reason of being traded on a secondary market (e.g. via a cryptocurrency exchange).
 - 2.1.2 **Non-Security Token:** A token which is deemed not to be a "security" will typically be either:
 - 2.1.2.1 a **utility token** - this confers on the holder merely a usage right or the right to access a product or service. Such a token has no economic rights attached to it, there is no expectation of a return.
 - 2.1.2.2 a **cryptocurrency token** - this is designed to behave like a currency, being a store of value and medium of exchange and referred to in some jurisdictions as a payment token.
- 2.2 As set out below, the JFSC will apply general requirements to all ICO Issuers irrespective of whether the token is a "security" for Jersey regulatory purposes. The JFSC reserves the right to consider each application on a case by case basis, however, the JFSC may consider relaxing certain conditions for non-security tokens in certain circumstances.

3 General requirements for all ICO Issuers

3.1 To ensure consistency and to provide a streamlined COBO application process, the following set of requirements will apply to all Jersey ICO issuers.

3.2 The issuer will need to:

- 3.2.1 be incorporated as a Jersey company with its registered office being provided by the TCSP appointed by the issuer
- 3.2.2 receive consent under the COBO from the JFSC before it undertakes any activity;
- 3.2.3 comply with the JFSC’s Sound Business Practice Policy;
- 3.2.4 apply relevant AML/CFT requirements to persons that either purchase tokens from, or sell tokens back to, the issuer of those tokens;
- 3.2.5 appoint and maintain a TCSP;
- 3.2.6 appoint and maintain a Jersey resident director who is a natural person and also a principal person of the TCSP appointed by the issuer;
- 3.2.7 be subject to an ongoing audit requirement;
- 3.2.8 have procedures and processes in place to (i) mitigate and manage the risk of retail investors investing inappropriately in the ICO, and (ii) to ensure retail investors understand the risks involved;
- 3.2.9 prepare and submit to the JFSC an Information Memorandum (which may be in the form of a White Paper) which complies with certain content requirements required of a prospectus issued by a company under the Companies (Jersey) Law 1991; and
- 3.2.10 ensure that any marketing material (including the Information Memorandum) is clear, fair and not misleading.

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The following press releases provide further reference:

- 1. States of Jersey -13 December 2017 - Initial coin offerings in Jersey,
<https://www.gov.je/News/2017/Pages/InitialCoinOfferings.aspx>
- 2. JFSC – 30 November 2017- warning on Initial Coin Offerings
<https://www.jerseyfsc.org/media/1612/jfsc-warning-initial-coin-offerings.pdf>
- 3. JFSC – 2 February 2018 - Statement on regulation of Initial Coin Offerings (ICOs) in Jersey
https://www.jerseyfsc.org/media/1719/2018-02-02_statement_on_regulatory_treatment_of_icos.pdf

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4 JFSC ICO Issuer Requirements

To ensure consistency and to provide a streamlined application process, the following application and ongoing requirements will apply to all Jersey-based issuers of ICOs².

These requirements relate only to the consent granted under the Control of Borrowing (Jersey) Order 1958 (**COBO**). In some cases the ICO or issuer may be subject to other laws or regulations in Jersey. Therefore, ICO issuers or potential ICO issuers need to consider all aspects of Jersey law and regulation that might apply.

Jersey company

4.1 The issuer would need to be incorporated as a Jersey company and not any other vehicle.

Prior JFSC consent and consent for material changes

4.2 The issuer needs to receive a COBO Consent from the JFSC before it undertakes any activity. As the issuer must be incorporated as a Jersey company, consent will be required under Article 2 (and also, where the token is a security, Article 4 of COBO).

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

4.3.1 Proposed activity including relevant timelines

4.3.2 Details of the issuer and the ICO

4.3.3 Rationale for the ICO, amount to be raised and use of proceeds

4.3.4 Summary of the features of the tokens

4.3.5 Summary of purchase and redemption processes

4.3.6 Service providers to the issuer

4.3.7 Relationship between issuer and holder of tokens

4.3.8 Management of underlying assets and security rights over such assets for holders of the tokens

4.3.9 How the activity will be wound up/dissolved and assets distributed to the holders of the tokens

4.3.10 Jersey legal and regulatory analysis (including consideration of relevant legislation or other regulatory laws)³ (together, the **Proposal**)

4.4 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 Proposal.

² The JFSC reserves the right to impose additional conditions on the issuer.

³ including, but not limited to COBO, Financial Services (Jersey) Law 1998, Banking Business (Jersey) Law 1991, Collective Investment Funds (Jersey) Law 1988, Alternative Investment Funds (Jersey) Regulations 2012, Companies (Jersey) Law 1991 and the Proceeds of Crime (Jersey) Law 1999), Proceeds of Crime (Supervisory Bodies) (Jersey) Law 2008.

Sound Business Practice Policy and AML/CFT requirements

- 4.5 The issuance of tokens is a sensitive activity falling within Table 2 of the Sound Business Practice Policy. Accordingly, the issuer shall maintain and adopt systems, controls, policies and procedures for customer take-on and redemption, profiling and transaction monitoring at enhanced levels ensuring internal and external reporting of suspicions of money laundering and financing terrorism activity.
- 4.6 The issuer shall be required pursuant to the relevant condition of the COBO consent granted to the issuer to undertake the following AML/CFT 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:
- 4.6.1 to establish and obtain evidence to verify identity; and
 - 4.6.2 to establish and depending on the level of risk obtain evidence to verify the source of funds and source of wealth.
- 4.7 Where the AML/CFT checks are not undertaken to the satisfaction of the TCSP appointed by the issuer, the tokens must not be issued to / purchased from the person.
- 4.8 The above measures are in addition to the existing obligations on a TCSP appointed by the issuer to comply with the relevant Jersey AML/CFT requirements with regard to the Issuer as its customer.
- 4.9 It is noted that there is yet no international standard regarding the application of AML/CFT requirements in respect of ICOs and the issuers of ICOs. However, a useful analogy can be applied in considering an issuer acting in a similar manner to an exchange conducting Money Service Business. Equally, typologies exist internationally that demonstrate that ICOs can be used in money laundering and terrorist financing worldwide and therefore Jersey must look to put in place suitable measures to protect the jurisdiction against this risk. It is the view of the Jersey authorities that in order to mitigate this risk, these AML/CFT controls are an appropriate measure – whilst monitoring if an international standard develops.

TCSP and Jersey resident director

- 4.10 The issuer must appoint and at all times maintain a TCSP.
- 4.11 The issuer must appoint and at all times maintain a Jersey resident director. The Jersey resident director must be an officer⁴ of the TCSP appointed by the issuer, who is a natural person and also a principal person of that business pursuant to the Financial Services (Jersey) Law 1998.
- 4.12 The issuer must seek the prior approval of the JFSC before changing the TCSP, the Jersey resident director or specified counterparties of the issuer as set out in the COBO consent.
- 4.13 Prior to a TCSP being appointed by the issuer, and on an ongoing basis it must take appropriate steps to satisfy itself as to:
- 4.13.1 The honesty and integrity of the issuer and the persons associated with it

⁴ A natural person

- 4.13.2 The issuer's approach to acting in the best interests and needs of each and all its customers
 - 4.13.3 The adequacy of the issuer's financial and non-financial resources
 - 4.13.4 How the issuer will manage and control its business effectively, and ensure that it will conduct its business with due skill, care and diligence
 - 4.13.5 The effectiveness of the issuer's arrangements in place for the protection of client assets and money when it is responsible for them
 - 4.13.6 The effectiveness of the issuer's corporate governance arrangements
 - 4.13.7 How the issuer ensures that that all systems and security access protocols are maintained to appropriate high standards
 - 4.13.8 What systems the issuer has in place to prevent, detect and disclose financial crime risks such as money laundering and terrorist financing
 - 4.13.9 The issuer's marketing strategy, including the types of persons to whom the ICO will be marketed, how it will be marketed, and the jurisdictions in which it will be sold or marketed (including consideration of any relevant laws or restrictions that may apply in other jurisdictions)
 - 4.13.10 The resilience of the issuer and the adequacy of contingency plans for the orderly and solvent wind down of its business.
- 4.14 The TCSP must ensure that it has the appropriate level of knowledge, skills and experience to appropriately carry out the above steps and to provide the agreed services to issuer, taking into account the activities carried on by the issuer. Compliance with this will be considered as part of the JFSC's supervisory approach to the TCSP sector.

Procedures and processes in place to (i) mitigate and manage the risk of retail investors investing inappropriately in ICOs, and (ii) to ensure retail investors understand the risks involved

- 4.15 The issuer of the ICO must take appropriate steps to mitigate and manage the risks of retail investors investing inappropriately in ICOs. The following safe harbour process must be applied where no other satisfactory process (e.g. minimum investment amounts or considering the appropriateness of the purchase to the person's circumstances) is agreed with the JFSC.
- 4.16 The issuer will be required to establish a process to ensure that the purchaser actively confirms that they are aware of and understand the risks of their investment. This will take the form of, as part of the token purchase process, the client being presented with the risk warning below and being required to confirm that they wish to proceed with the purchase. The risk warning and process for active confirmation must be presented together, with appropriate prominence, and in a form that does not contain any other information. The token should not be able to be sold to a person until they have actively confirmed their understanding of, and acceptance of, the risk warning.

Risk Warning: Token sales or coin offerings are typically a highly speculative form of investment. Investors should be prepared for the possibility of losing their investment completely. Investment in token sales or coin offerings is not subject to existing capital market regulations and protections.

I understand these risks and wish to proceed to purchase tokens or coins from [ISSUER NAME].

Audited annual accounts

- 4.17 The issuer of the ICO is to have its annual accounts audited and filed with the Registrar in accordance with Article 108 of the Companies (Jersey) Law 1991, irrespective of its status (whether public or private company).

Change of counterparties

- 4.18 There shall be no change in certain specified counterparties of the issuer without the prior approval of the JFSC.

Marketing materials

- 4.19 All marketing materials (including speeches and press statements) provided by the issuer must be clear, fair and not misleading.
- 4.20 The issuer is prohibited from directly or indirectly stating or implying any of the following:
- 4.20.1 That the issuer, or the coins or tokens issued by the issuer, are regulated by the JFSC
 - 4.20.2 The JFSC has, in any other way, considered or provided any level of assurance relating to the conduct or financial standing of the issuer, the tokens issued by it, or any project being carried on by the issuer
- 4.21 All written marketing materials (including press statements) referring to the regulatory treatment of the issuer or the tokens offered must either explain the regulatory treatment in the following manner or use the wording provided in Appendix 1:

Anyone issuing an ICO through a Jersey company will require a specific consent from the Jersey Company Registry, part of the Jersey Financial Services Commission. Whilst this consent does not give the ICO or the issuer a 'regulated' status, it mandates a set of conditions designed to ensure that the issuer meets specific standards in terms of governance, investor disclosure and AML/CFT compliance.

Prospectus / information memorandum

- 4.22 Prior to the issuance of any tokens, the issuer of the ICO is to provide to the JFSC, for confirmation of "no objection", marked "DRAFT", a copy of any proposed prospectus or information memorandum (which may be in the form of a White Paper) which must contain the information required under the Schedule to the Companies (General Provisions) (Jersey) Order 2002 and contain clear risk warnings highlighting that the ICO is unregulated and that it may result in substantial risks for investors. The risk warning must clearly state that : a) ICOs are typically a highly speculative form of investment; b) investors should be prepared for the possibility of losing their investment completely; and c) investment in token sales or coin offerings is not subject to existing capital market regulations and protections;
- 4.23 Not to publish the prospectus or information memorandum referred to in paragraph 4.22, above, until such time as the JFSC has issued confirmation of "no-objection";
- 4.24 not to regard, or to cause any third party to consider, any confirmation of "no objection" issued by the JFSC, pursuant to paragraphs 4.22 or 4.23 above, as the JFSC providing its agreement and/or consent to the Marketing Material issued by the ICO;

- 4.25 not to issue any coins or tokens until such time as the JFSC may have issued its confirmation of "no-objection" in respect of the matters identified in the paragraphs above; and
- 4.26 that a reference (if any) to the COBO consent in any prospectus or other invitation for subscription will refer to the consent having been granted by the JFSC under COBO and shall include the following statement:- "The Jersey Financial Services Commission is protected by the Control of Borrowing (Jersey) Law 1947, as amended, against liability arising from the discharge of its functions under that Law".

On-going reporting requirements to the JFSC

- 4.27 The board of directors of the issuer shall advise the JFSC promptly if it defaults on any token issued;
- 4.28 At the same time as submitting the issuer's Annual Return the directors shall provide a separate confirmation in the following format: "The directors having taken reasonable steps to ascertain the position, confirm that to the best of their knowledge there have been no breaches of the Article 2 Control of Borrowing (Jersey) Order 1958 consent and its conditions and, where relevant, the Company's Article 4 Control of Borrowing (Jersey) Order 1958 consent and its conditions, other than those (if any) previously disclosed to the Jersey Financial Services Commission".

APPENDIX 1

Statement which may be included in Marketing Materials

1 Jersey Treatment of Issuer

- 1.1 There are currently no existing capital markets regulations in Jersey specifically governing initial coin offerings (**ICOs**). However, the Jersey Financial Services Commission (the **JFSC**) is aware of the desire of ICO promoters to use a Jersey incorporated issuer because of Jersey's reputation as a well-regulated and reputable jurisdiction.
- 1.2 Accordingly, the JFSC has established certain conditions that any issuer of an ICO registered in Jersey is required to satisfy. These are implemented through a consent (a **COBO Consent**) granted under the Control of Borrowing (Jersey) Order 1958, which any Jersey entity wishing to issue an ICO must obtain.
- 1.3 The conditions require the issuer of the ICO to take certain measures to manage, amongst other things, financial crime and investor risks. The conditions reflect the guiding principles pursuant to which the JFSC discharges its functions as the Island's financial services regulator (**the Guiding Principles**) which are to have regard to:
 - 1.3.1 the reduction of the risk to the public of financial loss due to dishonesty, incompetence, malpractice or the financial unsoundness of financial service providers;
 - 1.3.2 the protection and enhancement of Jersey's reputation and integrity in commercial and financial matters;
 - 1.3.3 the best economic interests of Jersey; and
 - 1.3.4 the need to counter financial crime both in Jersey and elsewhere.
- 1.4 However, whilst the JFSC has established certain conditions that issuers of ICOs are required to satisfy, it does not regulate or supervise the ICOs or the issuers.
- 1.5 The COBO Consent imposes on the issuer certain requirements which reflect the Guiding Principles, including to:
 - 1.5.1 acknowledge that ICOs are a "sensitive activity" falling within the JFSC's Sound Business Practice Policy. Accordingly, the issuer must maintain and adopt systems, controls, policies and procedures for the customer take-on, profiling and transaction monitoring at enhanced levels ensuring reporting of suspicions of money-laundering and financing of terrorism activity;
 - 1.5.2 apply relevant AML/CFT requirements to persons that either purchase tokens from, or sell tokens back to, the issuer of those tokens;
 - 1.5.3 appoint and maintain a TCSP;
 - 1.5.4 appoint and maintain a Jersey resident director on the board of the issuer; where the Jersey resident director is a natural person and also a principal person of TCSP appointed by the issuer;
 - 1.5.5 obtain the JFSC's prior approval to any change to the TCSP appointed by the issuer, the Jersey resident director of the issuer or additional specified counterparties of the issuer as set out in the COBO consent;
 - 1.5.6 prepare and file annual audited accounts with the Jersey Companies Registry;

- 1.5.7 have procedures and processes in place to (i) mitigate and manage the risk of retail investors investing inappropriately in the ICO, and (ii) to ensure retail investors understand the risks involved;
- 1.5.8 prepare and submit to the JFSC an Information Memorandum (which may be in the form of a White Paper) which complies with certain content requirements required of a prospectus issued by a company under the Companies (Jersey) Law 1991; and
- 1.5.9 Ensure that any marketing material (including the Information Memorandum) is clear, fair and not misleading.