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Chapter 21

SWITZERLAND

Olivier Favre, Tarek Houdrouge, Grégoire Tribolet and Fabio Elsener[1]

I INTRODUCTION TO THE LEGAL AND REGULATORY FRAMEWORK

i Market size

Switzerland is the home of the crypto valley in Zug, near Zurich, and has an active community of enterprises working in the crypto space. While it is difficult to attribute a rank to Switzerland in the fast-moving global crypto community, Switzerland has taken the role of a pioneer in this area. It is an important jurisdiction for initial coin offerings (ICOs) and securities token offerings (STOs), and it offers a well-developed infrastructure and a sound legal framework for companies that are active in the crypto space.

ii Legal framework

Switzerland has a favourable and attractive legal framework regarding cryptoassets, although it does not have a separate legal framework for them. For cryptocurrencies, the regulatory framework allowing the issuance and trading of these assets has been in place for a few years. Switzerland has now improved its regulatory framework for tokens representing rights, such as asset tokens and utility tokens representing claims against the issuer or a third party, by adopting the Federal Act on the Adaptation of Federal Law to Developments in Distributed Ledger Technology (the DLT Act), which introduced various amendments to Swiss laws to take account of the potential offered by distributed ledger technology (DLT). The DLT Act has been fully in force since August 2021. In particular, the DLT Act introduced DLT rights as the digital alternative to certificated securities as a new class of assets. DLT rights should be exclusively transferable through the blockchain. In addition, a new type of licence category for trading venues where DLT rights could be traded has been introduced into Swiss law. Moreover, additional segregation rights for cryptoassets held in custody by a third party (e.g., by a wallet provider) have been introduced in case of bankruptcy of the third party.

The Swiss Financial Market Supervisory Authority (FINMA) has repeatedly stated that it will not distinguish between different technologies used for the same activity: that is, it will apply the principle of 'same business, same rules' to any kind of new technology. FINMA adheres to this principle at present when applying Swiss financial market laws to cryptoassets and blockchain-based applications.

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iii Regulatory classification of tokens

On 16 February 2018, FINMA published guidance on how to apply Swiss financial markets laws in its guidelines regarding the regulatory framework for ICOs (the ICO Guidelines).[2] In the ICO Guidelines, FINMA clarifies how to classify cryptocurrencies and other coins or tokens (collectively with cryptocurrencies, tokens) or other assets registered on distributed ledgers under Swiss law.

According to the ICO Guidelines, FINMA distinguishes the following categories of tokens:

a payment tokens or cryptocurrencies, which are intended only as means of payment and that do not give rise to any claims against the issuer;

b utility tokens, which provide rights to access or use a digital application or service, provided that the application or service is already operational at the time of the token sale; and

c asset tokens, which represent an asset, for instance a debt or equity claim against the issuer or a third party, or a right in an underlying asset.

FINMA has further clarified that tokens may also take a hybrid form, including elements of more than one of these categories. These hybrid tokens must comply cumulatively with the regulatory requirements applicable to each relevant token category. FINMA acknowledges that a token's classification may change over time. For the purpose of assessing the regulatory implications of an ICO, the moment of the token issuance is relevant. However, the initial classification may change post-ICO. In the event of any secondary market trading activity with tokens, their classification in the moment of the relevant trading activity must be taken into account.

In addition, FINMA published its views on the regulatory classification of stable tokens (i.e., tokens backed by an underlying asset such as a pool of fiat currencies or other assets) in a supplement to the ICO Guidelines dated 11 September 2019. FINMA specified that stable tokens are not considered a separate type of token category under Swiss regulation and that, depending on the rights attached to stable tokens, these would usually classify as asset tokens or as hybrid between payment tokens and asset tokens.

Payment tokens do not qualify as legal tender or other means of payment under Swiss law. However, the Swiss Federal Council has clarified that payment tokens may be used as private means of payment if the parties to a transaction agree on the use of payment tokens as the applicable means of payment for such a transaction. In addition, the issuance of payment tokens requires compliance with the Swiss anti-money laundering AML rules (see Section V).

iv Enquiries to FINMA

Notwithstanding the guidance provided by FINMA generically, it is also possible to approach FINMA with 'no-action' enquiries to confirm the regulatory classification of real-life projects. Given that this is a new field with constantly evolving structures for token offerings, it is standard practice to file such no-action letters to FINMA and wait with the go-live of a structure for the FINMA confirmation.

2 FINMA, Guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs) (available at https://www.finma.ch/en/~/media/finma/dokumente/dokumentencenter/myfinma/1bewilligung/fintech/wegleitung-ico.pdf?la=en).

II SECURITIES AND INVESTMENT LAWS

i Relevance for asset tokens and certain types of utility tokens

Swiss securities laws are relevant for the issuance of asset tokens or any hybrid form of tokens involving the functionality of asset tokens (e.g., a stable token or a utility token regarding the use of a platform that is not fully developed).

However, payment tokens and utility tokens that do not represent any claims against an issuer or a third party are not subject to Swiss securities laws, as they do not represent any rights.[3] Such payment tokens and utility tokens should be classified as intangible digital assets *sui generis* for the time being.[4]

ii Issuance of tokens representing rights against an issuer or a third party

The DLT Act introduced DLT rights (DLT Rights) as new class of assets into Article 973d et seq. of the Swiss Code of Obligations (CO) for asset tokens or utility tokens representing any claims against an issuer or third parties. DLT Rights are designed as digital equivalent of certificated securities or uncertificated securities by linking a right to a token instead of a certificated security instrument or a registration in an uncertificated securities register. DLT Rights may not be exercised or transferred outside the relevant distributed ledger. As regards the scope of DLT Rights, any rights that could be issued as certificated or uncertificated securities may be issued as DLT Rights. Therefore, they may be used to represent fungible contractual claims (e.g., debt obligations), non-fungible contractual claims (e.g., claims arising from a licensing agreement), membership rights that can be issued as certificated or uncertificated securities (e.g., shares in stock corporations), and rights *in rem* that can be issued as certificated or uncertificated securities (e.g., mortgage certificates). However, cryptocurrencies or the possession or factual control of assets could not be issued as DLT Rights.

According to the DLT Act, the issuance of DLT Rights requires the registration of a right on a distributed ledger based on an agreement between the issuer and the first holder stipulating the registration of the relevant rights on a distributed ledger and the undertaking that such rights may only be transferred and exercised on the relevant distributed ledger. In addition, it is advisable that the parties explicitly specify their intention in the terms of the DLT Rights to create DLT Rights and that Swiss law shall be the applicable law. Without such a choice of law, the Swiss Private International Law Act as amended by the DLT Act stipulates that the laws of the place of incorporation or residence of the issuer, subject to special rules for rights *in rem*, apply.

Moreover, the DLT Act specifies certain characteristics that have to be met by the distributed ledger on which a DLT Right is issued. Such a distributed ledger must provide the right to dispose over the DLT Rights only to the holders of the DLT Rights (and not the debtor), protect its integrity through appropriate technical and organisational measures against unauthorised access and changes, record or make accessible through the distributed ledger its terms of operations and the terms of the relevant DLT Rights, and ensure that the

3 Federal Council report, Legal framework for distributed ledger technology and blockchain in Switzerland, 14 December 2018, 63 (available at https://www.newsd.admin.ch/newsd/message/attachments/55153.pdf).

4 See Federal Council report, Legal framework for distributed ledger technology and blockchain in Switzerland (footnote 3) 50 and 63; Federal Council, Report on virtual currencies, 25 June 2014, 7 (available at http://www.news.admin.ch/NSBSubscriber/message/attachments/35361.pdf).

register entries on the distributed ledger are visible to the public. However, the DLT Act does not define any technical requirements, for example, regarding the minimum number of participants in the ledger or the applied consensus mechanism.

Finally, DLT Rights may be used as underlyings for the creation of book-entry securities pursuant to the Swiss Federal Act on Intermediated Securities (FISA) by transferring them to a custodian within the meaning of the FISA and by that custodian crediting the DLT Right to one or more securities accounts. The custodian has to immobilise the DLT Rights, which may only be transferred in accordance with the FISA once they are held as book-entry securities.

iii Transfer requirements for tokens

Under Swiss law, payment tokens and utility tokens that do not represent any claims against an issuer or third parties can be validly created and transferred in accordance with the terms of the respective distributed ledger. A transfer can therefore be validly made by executing a transaction between two wallets.

Asset tokens or utility tokens representing any claims against an issuer or third parties that are issued as DLT Rights, however, can only be transferred in accordance with the rules of the relevant distributed ledger. It is no longer relevant how the relevant rights represented in the DLT Right would be transferred without the digital representation in a DLT Right, as it is the case for any asset tokens or utility tokens representing any claims against an issuer or third parties that are not issued as DLT Rights. The DLT Act provides for a rule on the finality of such transfers even if the transferor falls into insolvency. Holders of DLT Rights will also benefit from bona fide protection rights similar to holders of paper-form security certificates in case they have acquired DLT Rights from an unauthorised seller.

iv Classification of tokens as securities

According to Article 2(b) of the Financial Market Infrastructure Act (FMIA), securities are certificated or uncertificated securities, derivatives, intermediated securities or DLT Rights, which are standardised and suitable for mass trading. According to Article 2(1) of the Financial Market Infrastructure Ordinance, 'standardised and suitable for mass training' means, in this context, that the instruments are offered for sale publicly in the same structure and denomination, or that they are placed with 20 or more clients under identical conditions.

FINMA has clarified in the ICO Guidelines that it will apply these rules in connection with tokens as follows:

Payment tokens do not qualify as securities given that they are designed to be used as means of payment according to FINMA. Payment tokens cannot fall under the definition of securities as they do not represent any rights that are exercisable against the issuer or third parties.

Utility tokens can qualify as securities if the platform where they can be used is not operationally ready at the time of the token sale, or if the tokens represent rights that may be enforced against the issuer or a third party. These utility tokens are deemed to have an investment purpose. FINMA further clarified that a case-by-case analysis is needed to clarify whether or not a utility token can be used for its intended purpose. In particular, it specifies that proof of concepts or beta versions of platforms or applications on which the utility tokens cannot (yet) be used would not suffice to fall outside the definition of securities for the purposes of the FMIA. However, on the basis that the qualification of tokens may

change over time, it is possible that utility tokens qualifying as securities will fall outside this definition once the platform where the tokens shall be used becomes fully functional for its intended purpose.

Asset tokens qualify as securities provided that they have been offered publicly or to 20 or more persons for sale.[5]

FINMA has stated that any enforceable rights of investors to receive or acquire tokens in the future resulting from a presale, for instance under a simple agreement for future tokens, qualify as securities if the rights have been offered publicly or on identical terms to more than 20 persons. However, the rights issued in the context of a presale do not constitute securities if the terms used in the presale are not standardised or different terms are used with each investor: for example, by varying the amount of rights, the pricing or any lock-up provision.

v Prospectus requirement

Regardless of the classification of tokens as securities, in respect of any tokens constituting a digital representation of rights that are exercisable against an issuer, the question arises of whether the tokens are subject to a prospectus requirement under the Swiss Financial Services Act (FinSA). Under the FinSA, a prospectus requirement applies, generally speaking, for all public offerings of securities, including tokens qualifying as securities (see Section II.iv).

In addition, as regards financial instruments offered to retail investors, the FinSA introduced an obligation to prepare a key investor document as an additional disclosure document in a similar way as currently applicable in the European Union pursuant to the Packaged Retail and Insurance-based Investment Products Regulation. This new obligation also applies to certain types of tokens qualifying as financial instruments (e.g., asset tokens with the economics of a structured product or a derivative).

vi Regulatory implications of classification of tokens as securities

If tokens qualify as securities, they are subject to the regulatory framework of the FinSA and the Financial Institutions Act (FinIA). According to this regulatory framework, a licence as a securities firm is required for any brokerage activities on behalf of clients (other than institutional clients) regarding such tokens and any market-making activities regarding such tokens.[6] Furthermore, underwriting such tokens and issuing tokens that qualify as derivatives are subject to a licence requirement as a securities firm or bank, if these activities are conducted on a professional basis.[7] A licence requirement is triggered in each case if these activities are executed on a professional basis.

Moreover, the qualification of tokens as securities has implications for the licence requirements under the FMIA for any secondary trading platform where such tokens can be traded.

vii Laws on collective investments

As regards any investments in tokens through collective investment schemes or funds or in regard to the issuance of tokens representing units in collective investment schemes, the rules of the Swiss Collective Investment Schemes Act (CISA) and its implementing ordinances

5 See Section 3.1 of the ICO Guidelines.

6 Article 41 FinIA.

7 cf. Article 44(1)(c) and (d) FinIA.

must be taken into account. For the purposes of the CISA, a collective investment scheme is a pool of assets raised from investors for the purpose of being invested collectively managed on behalf of the investors. The regulation of the CISA applies irrespective of the legal structure that has been chosen for the collective investment scheme or fund.

As a result, the issuance of tokens, as well as any business activity in relation to tokens (regardless of their classification) by which assets accepted from clients for investment purposes are pooled (i.e., there is no segregation of the investments for each investors), or where the clients' assets are managed by a third party on behalf of those clients, could be subject to the requirements of the CISA and the FinIA, and must be analysed from the perspective of the Swiss regulation of collective investment schemes.

Commercial undertakings generally do not fall within the scope of the CISA. However, it is only possible to draw the line between a commercial undertaking and a collective investment scheme on a case-by-case basis.

III BANKING AND MONEY TRANSMISSION

According to the Swiss Banking Act (SBA), a banking licence requirement is triggered if a company conducting primarily a financial activity accepts deposits from the public (i.e., from more than 20 persons) or publicly advertises this activity. According to the Swiss Banking Ordinance (SBO), entering into any liabilities would generally qualify as a deposit-taking activity, unless one of the exceptions defined in Article 5(2) and (3) SBO applies.

In the context of token sales, the most relevant exemptions are the following:

a to the extent that the liabilities are debt securities issued as standardised products suitable for mass trading or non-certificated rights with a similar function and the creditors are provided with disclosures (e.g., in a prospectus or private placement memorandum), including the minimum content as described in Article 5(3)(b) SBO at the time of the offer, the liabilities do not qualify as deposits; and

b to the extent that the liabilities arise from client funds held on settlement accounts with securities firms, asset managers or similar financial intermediaries, provided that the funds are used to settle client transactions, no interest is paid on the funds and – except for accounts with securities firms – the settlement occurs within 60 days at the latest.

Swiss law provides for a sandbox exemption pursuant to Article 6(2) SBO. According to this exemption, the acceptance of deposits from the public (i.e., from more than 20 persons) up to a maximum amount of 1 million Swiss francs is permitted without a banking licence, provided that no interest income is generated with the deposited amounts and the investor has been informed before accepting the deposit that the accepting person or entity is not subject to prudential supervision by FINMA, and that the investments are not protected by any deposit protection scheme.

Moreover, entities accepting deposits from the public up to a maximum of 100 million Swiss francs, provided that these deposits are not reinvested and they are not interest-bearing, may request a banking licence 'light'. Compared with a full banking licence, certain carve-outs apply regarding organisation, risk management, compliance, the qualifications of the regulatory auditor and the capitalisation requirements. The banking licence light has been available since 1 January 2019. It may be an interesting option for entities active in the crypto space that intend to take deposits from the public in an amount below the cap of 100 million Swiss francs.

When providing storage services regarding tokens, the following question arises: under what circumstances does the activity require a banking licence or a banking licence light? This would be relevant when the storage provider does not hold tokens with a payment function on a segregated basis (e.g., on individual public addresses for each client), but on an omnibus client account (e.g., on a shared public address for more than one client) as such storage activity on omnibus client accounts requires a banking licence or banking licence light.

With regard to brokerage services provided in respect of tokens, this activity could be subject to a banking licence if the service provider accepts fiat currencies or tokens on own accounts, respectively public keys, in connection with such services. In this event, the service provider would need to rely on the settlement account exemption mentioned above. However, this exception is not available to cryptocurrency traders that execute an activity comparable to foreign exchange traders (i.e., that expose their clients to similar bankruptcy risks as foreign exchange traders do).

IV ANTI-MONEY LAUNDERING

i Applicable rules

Under Swiss law, AML regulation consists of the Swiss Anti-Money Laundering Act (AMLA) and the Anti-Money Laundering Ordinance (AMLO). The AMLA applies, inter alia, to financial intermediaries. In addition to entities subject to prudential supervision, in brief, anyone accepting, holding or depositing assets belonging to other persons or assisting in the investment of such assets on a professional basis qualifies as a financial intermediary according to Article 2(3) AMLA. Furthermore, the AMLA contains a non-exhaustive list of activities that are considered financial intermediation. In the context of ICOs and tokens, the issuance of means of payment that cannot be used exclusively with the issuer,[8] providing services related to payment transactions in the form of money and asset transmission services,[9] and money exchange services[10] are relevant financial intermediation activities.

A financial intermediary within the meaning of the AMLA must be affiliated with an authorised AML self-regulatory organisation (SRO). Furthermore, a financial intermediary has to comply with the obligations defined in the AMLA, including, without limitation, identification and know-your-customer (KYC) obligations relating to the contracting party and its beneficial owner, and has to file reports to the Money Laundering Reporting Office Switzerland in cases of suspected money laundering or terrorism financing.

In the FINMA Guidance 02/2019 on payments on the blockchain dated 26 August 2019, FINMA specified that financial intermediaries supervised by FINMA must comply with the travel rule for blockchain transactions. This also applies to other financial intermediaries for AML purposes, as a result of their SRO affiliation.

Under the travel rule, the relevant Swiss financial intermediary has to transmit the same information as required for wire transfers in fiat money or, alternatively, it must:

a identify the transferee in accordance with the Swiss AML rules as if the transferee was a client of the Swiss financial intermediary; and

b verify the transferee's power to dispose of the wallet address used by it through appropriate technical measures as defined by the relevant Swiss financial intermediary.

8 See FINMA Circular 2011/01, Financial intermediation according to AMLA, n 64.

9 See Article 4(2) AMLO.

10 See Article 5(1)(a) AMLO.

ii ICOs

Depending on the classification of the tokens to be issued within an ICO, the issuance can qualify as financial intermediation activity. FINMA provides clarity in its ICO Guidelines on this matter, as outlined below.

The issuance of payment tokens is classified as an issuance of means of payment and therefore constitutes a financial intermediation activity pursuant to the AMLA.

The issuance of utility tokens that constitute some form of payment function on the designated application or platform (for example, the ability to use the utility tokens to pay for services used on such platform) usually qualifies as an issuance of means of payment and therefore constitutes a financial intermediation activity pursuant to the AMLA. However, the issuance of utility tokens does not qualify as financial intermediation if a utility token does not have any form of payment function or if the payment function is exceptionally considered as an ancillary function of the utility tokens.[11] To benefit from such an exception, it is required that the utility tokens' main purpose is to provide access rights to a non-financial application, that the entity providing the payment functionality is also the entity operating the non-financial application and that the access to the non-financial application could not be granted without including the ancillary payment functionality embedded in the utility token. However, note that FINMA applies this exception very restrictively, and in practice, any utility token with some sort of payment function is considered as a financial intermediation within the scope of the AMLA.

The issuance of asset tokens does not qualify as financial intermediation activity pursuant to the AMLA, provided that the asset tokens are classified as securities, and provided further that they are not issued by a bank, securities firm or certain other prudentially supervised entities. However, in practice, issuers of asset tokens are often required to conduct some KYC and identification processes on a voluntary basis owing to the compliance requirements of the banks to which the proceeds of the ICO will be transferred.[12]

The issuance of rights to acquire tokens in the future within a pre-ICO does not constitute a financial intermediation activity, provided that the issuer is not a bank, securities firm or certain other prudentially supervised entities. However, the subsequent issue of tokens that qualifies as issuance of a means of payment under the AMLA (i.e., payment tokens and, subject to the mentioned exceptions, utility tokens) to pre-ICO investors qualifies as financial intermediation. In consequence, the obligations arising from the AMLA are triggered in the moment of issuance.

In connection with ICOs that fall within the scope of the AMLA, FINMA specifies that obligations arising under the AMLA (e.g., KYC) can be outsourced to financial intermediaries in Switzerland that are affiliated with an SRO or under FINMA supervision, provided that any funds from the ICO are accepted via the financial intermediary; that is, any tokens or fiat currencies paid by investors have to be transferred to the public keys or accounts of the outsourcing partner before being transferred on to the relevant issuer.

11 ICO Guidelines, Section 3.6; FINMA Circular 2011/01, Financial intermediation according to AMLA, n 13 et seq.

12 See Swiss Bankers Association, SBA guidelines on opening corporate accounts for blockchain companies, September 2018 (available at https://www.swissbanking.ch/en/news-and-positions/press-releases/opening-corporate-accounts-for-blockchain-companies-swiss-bankers-association-publishes-guidelines-for-its-members).

iii Exchange and intermediation services

Exchanging fiat currencies against tokens or vice versa or exchanging two different tokens constitutes a financial intermediation activity subject to the AMLA.

If a service provider offers the exchange services directly (i.e., acts as an exchanging counterparty to its clients), this activity qualifies as money exchange under the AMLO. For these services, a *de minimis* threshold of 1,000 Swiss francs applies if the exchange operations involve cryptocurrencies, and transactions below this threshold are exempted from KYC or identification obligations under the AMLA.[13]

If a service provider offers exchange services with the involvement of a third party (e.g., an exchange platform for tokens), or if the service provider intermediates services relating to the transfer or exchange of tokens or fiat currencies and is involved in the payment process, the services qualify as money and asset transmitting services pursuant to Article 4(2) AMLO and the service provider qualifies as a financial intermediary under the AMLA.

Moreover, FINMA has specified in relation to the provision of payment service providers by institutions under its supervision that transfers of cryptoassets to external wallets (i.e., to wallets administered by third parties) are only allowed if the recipient wallet address belongs to one of its own clients, which has to be verified.[14] FINMA justifies this approach by the fact that there are currently no possibilities on blockchains to provide identifying information on the sender and recipient of a transaction similar to traditional wire transfers (e.g., via SWIFT).

iv Storage services

A storage services provider qualifies as a financial intermediary if it has the power to dispose of the private keys of the stored tokens (custodian wallets). Furthermore, this activity could trigger a banking licence requirement (see Section IV).

V REGULATION OF EXCHANGES

i Tokens qualifying as securities

In 2021, the DLT Act introduced a new licence category for trading platforms where DLT rights qualifying as securities (see Section II.vi) are traded. The legislature thereby departs from its principle of a technology-neutral regulation to remove the barriers that were preventing the establishment of trading venues to trade tokens qualifying as securities in Switzerland (at least for as long as such DLT securities were not structured as book-entry securities). Under the former licensing options, trading venues could not integrate post-trading activities into the trading platform. In addition, separate central counterparties and central securities depositories were required for the clearing and settlement of transactions. As regards transactions on distributed ledgers, post-trading activities of this kind are typically executed simultaneously with a transaction through registration of the relevant transaction on the distributed ledger without the involvement of additional intermediaries handling the clearing or settlement. In addition, the trading venues were not permitted to provide direct access to retail clients.

13 See Article 51a FINMA Anti-Money Laundering Ordinance for entities that are subject to FINMA supervision or the relevant regulations of the SROs.

14 See FINMA Guidance 02/2019, Payments on the blockchain, 26 August 2019.

The DLT Act amended the FMIA by introducing DLT trading systems as platforms providing for multilateral trading of DLT Rights or other foreign law-governed rights that are represented on a distributed ledger qualifying as securities based on non-discretionary rules (collectively, the DLT Securities) and that meet at least one of the following requirements: (1) the trading system allows trading by unregulated entities or individuals as participants; (2) the operator of the trading system deposits centrally the DLT Securities in accordance with a distributed ledger based on uniform rules; or (3) the operator of the trading system performs the post-trading activities with DLT Securities (e.g., clearing and settlement) based on uniform rules and procedures.

Moreover, the DLT Act allows a firm regulated as a securities firm or as a bank to operate an organised trading facility for the trading of DLT Rights.

ii Other tokens

In regard to the regulation of exchanges for payment tokens and utility tokens that do not qualify as securities, there are no licence requirements under Swiss law to operate businesses of this kind other than ensuring compliance with Swiss AML requirements (see Section V). However, as the operation of such exchanges usually implies the acceptance of fiat currencies or such tokens on accounts or public keys of the exchange operator, a banking licence requirement could be triggered as an acceptance constituting an acceptance of deposits from the public (see Section IV).

Similarly to the provision of brokerage services, an exchange may benefit from the exemption for settlement accounts if the clients' funds accepted on own accounts or public keys are used solely for the execution of trades on the exchange, are not interest bearing and are transferred on within 60 days. This exemption would only be applicable if the clients were not exposed to an increased bankruptcy risk, similarly to clients of a foreign exchange trader (see Section IV).

An exchange can benefit from the sandbox exception pursuant to Article 6(2) SBO if fiat currencies and tokens with a value of less than 1 million Swiss francs are accepted from the exchange participants and if the participants are informed of the absence of any prudential supervision over the exchange operator and any protection from a deposit protection scheme. In any event, the operation of an exchange for tokens constitutes a money and asset transmitting service pursuant to Article 4(2) AMLO. Therefore, an exchange operator qualifies as a financial intermediary that is, in particular, subject to the affiliation obligation with an SRO or a requirement to be licensed as a financial intermediary by FINMA.

VI REGULATION OF MINERS

i Role of mining and staking in virtual currency

In an unrestricted decentralised network (such as the Ethereum or Bitcoin blockchain), the creation of native tokens of the relevant distributed ledger, usually a payment token, plays an essential role in the record-keeping of transactions on the distributed ledger as there is no central authority monitoring transactions. To secure financial transactions and ensure that there is no fraud, validators must verify transactions and add them to the distributed ledger.

Usually, anyone participating in the entire ecosystem of the distributed ledger can become a validator and partake in the creation of new tokens in accordance with the rules of the relevant distributed ledger. Currently, there are two predominant concepts for validation, proof-of-work (also known as mining, used for Bitcoin) and proof-of-stake (used

for Ethereum). In proof-of-work, for each block of transactions, miners use mathematical protocols to verify transactions and validate them before sharing the result across the entire network. In proof-of-stake, the validator puts up a stake, a collateral in form of tokens, to earn the right to validate new blocks. The stake is immobilised for the duration of the process. In case of a wrong validation that is not congruent with the other validations within the network, the stake is destroyed in a process called slashing. This incentivises validators to act truthfully and protects the integrity of the blockchain. In both cases, the validation process creates virtual currency as the validators are awarded with new tokens for their activity.

ii Regulatory framework

There is no specific legislation addressing the regulatory status of validators in Switzerland. The validation process (including the self-issuance of tokens that do not qualify as derivatives) does not trigger a licence requirement under Swiss law per se. In practice, however, the activities of validators require a licence if they perform a regulated activity as described in Sections II to V. We note in this connection that, in particular, stalking activities may require a banking or banking licence light if they involve a deposit-taking activity or storage of cryptocurrencies on omnibus client accounts.

The self-issuance of tokens qualifying as securities is generally not subject to a licence requirement as a securities firm under the FinIA. This conclusion also holds true in the unlikely event that the tokens would qualify as derivatives provided that there is no offer of these derivatives to the public on a professional basis.

iii FINMA scrutiny and enforcement proceedings in connection with mining

FINMA generally has a favourable approach towards blockchain technology, but it cautiously monitors all market participants to ensure that the Swiss blockchain network remains free of fraud, in particular in the context of ICOs. It regularly highlights the risks involved for investors, and is committed to take actions against ICO business models violating or circumventing regulatory laws.

An example is the launch in July 2018 of enforcement proceedings by FINMA against Envion AG, a Swiss mining company, for a breach of Swiss financial regulations in the context of its ICO. This resulted in FINMA ruling that the company conducted a deposit-taking activity without being duly licensed as a bank[15] and ordering that the company enter bankruptcy liquidation.

As the regulatory status of activities in connection with the validation of tokens may raise some issues, a no-action letter from FINMA, for example with regard to specific activities of a validator, is always advisable to obtain legal certainty that the contemplated activity complies with all regulatory laws (see Section II.iv).

VII REGULATION OF ISSUERS AND SPONSORS

i Issuers

In regard to the legal form for issuers of tokens, two types of forms are generally used: a foundation and a joint-stock corporation.

15 https://www.finma.ch/en/news/2019/03/20190327---mm---envion/.

A foundation offers the complete independence and control of the board of the foundation as there are no shareholders. However, its assets must be used in line with the purpose of the foundation as stated in the deed of foundation. Therefore, the distribution of profits is limited to that purpose and it is not possible to distribute profits to the founders. In addition, every foundation is further subject to governmental supervision. Note that certain tax exemptions are available for foundations or stock corporations with either public or non-profit purposes. However, the conditions for obtaining such exemptions are very restrictive and are usually not met by entities pursuing an ICO.

In the context of an ICO, to the extent that there is, at least partially, a commercial purpose, and the issuer is not pursuing a non-for-profit purpose, the legal form of the Swiss foundation is most of the time not suitable. Its rigid structure does not allow for the flexibility that is generally needed, in particular as the founders have no ownership or any other control over the foundation's assets or funds and have no legal means to influence the foundation's conduct of business. Instead, a joint-stock corporation is the more suitable type of corporate form for issuers of ICOs.

An issuer of an ICO incorporated as a joint-stock corporation must have – unless it is incorporated with a contribution in kind – a paid-in capital of 50,000 Swiss francs (with a minimum share capital of 100,000 Swiss francs) deposited with a Swiss bank. However, following the incorporation, there is no restriction as to the place where the account is held. The issuer may also have an account with a foreign bank.

The issuer must comply with the regulatory requirements, to the extent applicable to the issuer, as set out in Sections II to VI.

Depending on the classification of the tokens issued, an issuer of tokens may be subject to the AMLA if it carries out financial intermediation activities (see Section V.ii). In the context of ICOs and tokens, the issuance of means of payment that cannot be used exclusively with the issuer, the provision of services related to payment transactions in the form of money and asset transmitting services or money exchange services are, for example, financial intermediation activities (see Section V).

ii Sponsors

As long as there is no activity performed falling within the scope of the regulated activities described in Sections II to VI, the sponsorship of tokens – including the marketing, publicity and promoting of tokens – is currently not subject to licence requirements in Switzerland.

However, this is conditional on the following:

a licence requirement under the SBA or the FinIA: if the sponsored company has a foreign regulatory status as a bank or securities firm because it has the relevant regulatory status under foreign legislation, it carries out activities qualified as banking or dealing in securities under Swiss legislation or it uses the terms 'bank' or 'securities firm' in its company name, any marketing activities in or from Switzerland for that foreign bank or broker-dealer – provided that such activities are performed by individuals engaged in Switzerland, on a professional and permanent basis – may bring the foreign bank or broker-dealer within the scope of a FINMA branch office or representative office licensing requirement; or

b prospectus requirement: the public offering of tokens, if they qualify as securities in accordance with the FinSA.

VIII CRIMINAL AND CIVIL FRAUD AND ENFORCEMENT

In Switzerland, fraudulent acts in connection with cryptocurrencies that are either committed in Switzerland, involve Swiss victims or have another nexus to Switzerland may result in criminal consequences as well as civil liability pursuant to the relevant provisions of Swiss law and potentially other applicable laws (e.g., civil liability pursuant to the chosen law for a specific business relationship). In addition, FINMA may start administrative enforcement proceedings and impose administrative consequences against entities with a Swiss presence for regulatory misconduct.

While any civil liability claims have to be brought before a competent court or arbitral tribunal in Switzerland by a claimant, criminal liability will be investigated by a public prosecutor either upon receiving evidence of a criminal offense by a victim, a third person or by any public authority. Please note that public authorities are typically obliged to report evidence for criminal activities to the competent criminal authorities.

Further, violations of regulatory requirements often result in criminal liability. If FINMA finds evidence for such criminal misconduct within its administrative proceedings (e.g., proceedings relating to regulatory misconduct or licensing proceedings), it will have to notify the competent criminal authorities.

IX TAX

In December 2021, the Swiss Federal Tax Administration (FTA) updated its working paper on the tax treatment of cryptocurrencies and ICOs for wealth, personal income and corporate income tax purposes as well as for withholding tax and stamp duty purposes.[16] The practice described in this working paper is set out below. However, this is only a snapshot and not all tax questions relating to cryptocurrencies or ICOs have yet been addressed and answered conclusively. Consequently, it is possible that the practice of the tax authorities described below may continue to develop and may change. It is therefore highly recommended to obtain advance tax rulings from the responsible tax authorities before performing an ICO.

Furthermore, the following explanations are limited to the tax consequences for issuers domiciled in Switzerland who have issued coins or tokens with monetary rights against any counterparty in the form of asset tokens and utility tokens.

Finally, the tax treatment of the tokens at investor level as well as the tax treatment of cryptocurrencies in the form of pure digital means of payment (native tokens or payment tokens) is not addressed.

i Taxation of asset tokens

Asset tokens represent rights of the investor in relation to the issuer, which consist of fixed compensation or of a certain, predetermined participation of the investor in a reference value (e.g., earnings before interest and taxes (EBIT)) of the issuer's business. The tax classification of asset tokens thus depends largely on the civil law structure of the legal relationship.

The updated working paper divides asset tokens into the following three subcategories for tax purposes:

16 This working paper was published in German, French and Italian (available at: https://www.estv.admin.ch/estv/de/home/direkte-bundessteuer/fachinformationen-dbst/kryptowaehrungen.html).

a Debt tokens: these tokens represent the legal or factual obligation of the issuer to repay all or a substantial part of the investment and, where applicable, to make an interest payment.
b Asset tokens with a contractual basis (formerly named equity and participation tokens): these tokens are issued against cash payment are measured by a certain ratio to profit or liquidation result, or a proportional share of a reference value of the issuer (e.g., EBIT, licence income or sales), and are regarded as derivative financial instruments.
c Asset tokens with participation rights: these tokens are issued in accordance with the law governing companies limited by shares (Article 620 seq. CO). They convey their holders' participatory rights as stipulated in the respective company's statutes.

In the following, the tax treatment of these three types of asset tokens for the issuer is described, assuming that the issuer is a corporation with tax residence in Switzerland.

Debt tokens qualify as bonds for tax purposes and are therefore treated as follows:

a Corporate income tax: the funds received from collective fundraising do not constitute taxable income and are recognised as liabilities in the issuer's balance sheet. Any interest payments to the investors are generally business expenses and are therefore tax deductible.
b Withholding tax: both periodic and one-off interest payments on debt tokens are subject to withholding tax at 35 per cent. Whether, and if so to what extent, a refund of the withholding tax is possible depends on the individual investor.
c Stamp duties: the issue of debt tokens is exempt from the securities transfer tax. In contrast, secondary market dealings in debt tokens are generally subject to the securities transfer tax at a rate of up to 0.15 per cent of the purchase price of the debt tokens; however, this is only if a securities dealer in Switzerland or Liechtenstein, as defined in the Stamp Duty Act, is a party or acts as an intermediary to the transaction and no exemption applies.

Asset tokens with a contractual basis are regarded as derivative financial instruments for tax purposes and are therefore treated as follows:

a Corporate income tax: funds raised through the issuance of asset tokens with a contractual basis qualify as taxable income and are recognised as income in the issuer's income statement. If the issuer has made a contractual commitment to implement a specific project, a provision can be booked as an expense, which reduces the taxable income accordingly. Provisions that are no longer required after completion of the project development are to be released to the income statement. Payments to the investors based on their entitlement to a certain share of the profit or liquidation result (or both) generally qualify as tax-deductible expenses. However, this assumes that the investors are known at the time of payment, that the issuer's shareholders do not hold more than 50 per cent of the issued tokens and that the payments to the token holders do not exceed 50 per cent of EBIT. If these conditions are not met, there is a taxable hidden profit distribution.
b Withholding tax: asset tokens with a contractual basis or payments thereof are not subject to withholding tax; however, if the issuer's shareholders hold more than 50 per cent of the issued tokens and the payments to the token holders amount to more than

50 per cent of EBIT, the FTA assumes – as already mentioned above – a hidden profit distribution, which is subject to withholding tax. In the event of any tax evasion, the FTA also reserves the right to levy withholding tax.

c Stamp duties: the issue of asset tokens with a contractual basis is not subject to the issuance stamp tax, as the asset tokens with a contractual basis tokens do not qualify as participation rights within the meaning of the Stamp Duty Act. In the case of asset tokens with a contractual basis purchased by the issuer's shareholders, the question arises of whether the payment represents a taxable contribution or not. This depends on whether or not the purchase price paid for the asset tokens with a contractual basis represents a corresponding consideration. If there is such a consideration, there is no taxable contribution; however, without such a consideration, there is a taxable contribution subject to 1 per cent issuance stamp tax. Derivative financial instruments regularly do not qualify as taxable securities within the meaning of the Stamp Duty Act, which is why secondary market transactions are not subject to securities transfer tax.

Asset tokens with participation rights are qualified and treated as shares or other equity securities:

a Corporate income tax: funds raised through the issuance of tokens with participatory rights do not constitute taxable income, insofar as they qualify as capital contributions, including premium and *à-fonds-perdu* payments.

b Withholding tax: payments to holders of tokens with participatory rights qualify as dividends and are therefore subject to withholding tax.

c Stamp duties: the issuance of asset tokens with participation rights is subject to issuance stamp tax. In the amount that the purchase price for a token with participatory rights does not represent a corresponding consideration, it is regarded as a taxable contribution subject to issuance stamp tax.

ii Taxation of utility tokens

For the purpose of the tax analysis below, it is assumed that the issuer undertakes to use the funds received from the sale of utility tokens exclusively for developing the digital service and to enable investors to access or use the service. The issuer has no further obligations to the investors. Utility tokens are basically to be classified as a contractual relationship between the issuer and the investor to use a corresponding DLT service. The mandate is that the issuer must act in accordance with the contractual agreement between itself and the investors. Accordingly, utility tokens are treated as follows for tax purposes:

a Corporate income tax: funds raised through the issuance of utility tokens qualify as taxable income and are recognised as income in the issuer's income statement. If the issuer has made a contractual commitment to implement a specific project, a provision can be booked as an expense, which reduces the taxable income accordingly. Provisions that are no longer required after completion of the project development are to be released to the income statement.

b Withholding tax: claims arising from contractual relationships are not subject to withholding tax. Accordingly, the right to use the digital services does not constitute income subject to withholding tax.

c Stamp duties: the issue of utility tokens is not subject to the issuance stamp tax, as the utility tokens do not qualify as participation rights within the meaning of the Stamp Duty Act. In the case of utility tokens purchased by the issuer's shareholders,

the question arises of whether the payment represents a taxable contribution or not. This depends on whether or not the purchase price paid for the utility tokens represents a corresponding consideration. If there is such a consideration, there is no taxable contribution; however, without such a consideration, there is a taxable contribution subject to 1 per cent issuance stamp tax. Utility tokens do not qualify as taxable securities within the meaning of the Stamp Duty Act, which is why neither the issuance of, nor secondary market dealings in, utility tokens are subject to securities transfer tax.

d Value-added tax: in contrast to native and asset tokens, the issue of utility tokens is generally subject to value-added tax.

X LOOKING AHEAD

The DLT Act removed some of the most significant obstacles to the development of a functioning primary and secondary market in digital assets in Swiss law and created a sound legal basis for issuing and trading rights represented in tokens. The impact of the new possibilities introduced by the DLT Act in practice has to be observed going forward. However, for cross-border issuances, the impact of the new legislation may be limited in the future by new legislation currently under way in other relevant markets, such as the proposal for an EU regulation on markets in cryptoassets (known as MiCA) that was adopted by the European Parliament on 20 April 2023 which is expected to enter into force in July 2024 and January 2025. Besides issuances, it also covers all services related to crypto provided in the EU. This may impose additional requirements for distributing tokens issued in Switzerland within the European Union.