

## The stablecoin supplement of 2019

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On 11 September 2019 FINMA published a supplement to its ICO guidelines dealing with stablecoins, tokens whose value is linked to an asset such as a currency, a commodity, real estate or securities. FINMA stated that it would apply the principles of "substance over form" and "same risks, same rules". The legal qualification of a stablecoin depended on the rights that its holders acquired against the issuer or a third party and on the nature of the underlying asset. Where a token was linked to a specific fiat currency with a fixed redemption claim, such as one token for one franc, FINMA considered a classification as a deposit under banking law indicated. Where the link was to a basket of assets managed for the account and at the risk of the holders, with a pricedependent redemption claim, a collective investment scheme was probable. A token linked to commodities that merely evidenced the holder's ownership right generally did not qualify as a security, whereas a purely contractual claim against the issuer pointed to a deposit in the case of bank precious metals and, for other commodities, to a security and possibly a derivative.<sup>1</sup>

The supplement was published together with FINMA's response to an enquiry by the Libra Association in Geneva, the consortium that Facebook had formed in June 2019 to issue a global stablecoin. FINMA stated that the project as described would require a licence as a payment system under the Financial Market Infrastructure Act (FMIA), that it would fall under the anti-money laundering rules and that its reserve management would have to meet requirements comparable to those of banks. FINMA also required that the returns and risks of the reserve be borne entirely by the association, which left the token holders without exposure to them.<sup>2</sup> The Libra project was renamed Diem in December 2020, and in January 2022 the Diem Association wound it down and sold its assets to Silvergate Capital. FINMA's analysis nevertheless anticipated a theme that would return in 2024 and 2025: a stablecoin that promises redemption at par performs a monetary function and must be regulated in proportion to that function.

## 1 Early enforcement against unauthorized offerings

FINMA's enforcement practice confirmed the guidelines. The best documented case concerns a company that conducted an ICO in 2017 and 2018 in which it collected assets from about 37,000 investors with a value of more than CHF 90 million and issued tokens that it described as bonds. In its ruling of 15 March 2019 FINMA found that the company had accepted public deposits on a commercial basis without a banking licence and had thereby seriously violated Article 1 paragraph 2 of the Federal Act on Banks and Savings Banks of 8 November 1934 (Banking Act, BankA), SR 952.0. The Federal Administrative Court refused to hear an appeal on 2 March 2021, so that the ruling became final.<sup>3</sup> The company had promised the token holders a share of its profits and a contractual right that resembled a claim for repayment. Because the tokens did not meet the requirements of a bond under banking law, the exemption for bonds did not apply. The media release of 27 March 2019 named the company as envion AG, which had issued EVN tokens against payments in US dollars, ether and bitcoin and which the Cantonal Court of Zug had placed in bankruptcy in March 2019, so that the liquidation passed to the Zug bankruptcy office.<sup>4</sup>

The case showed that the label which an issuer gives to its token decides nothing. FINMA examined the obligations that the issuer had assumed and found that they amounted to deposits, regardless of the technology. For Ticino practice the lesson was that a token sale which promises investors a fixed or variable return without a prospectus-compliant bond structure or a banking licence exposes the issuer and its directors to the full range of enforcement measures under Articles 31 to 37 of the Financial Market Supervision Act (FINMASA), including liquidation and bankruptcy. Directors and managers can also face criminal proceedings by the Federal Department of Finance under Article 44 FINMASA for activity without authorization.

## 2 Notes

1. FINMA, media release "FINMA publishes 'stable coin' guidelines", 11 September 2019, <https://www.finma.ch/en/news/2019/09/20190911-mm-stable-coins/> (underlying assets: currencies, commodities, real estate, securities; "substance over form"; "same risks, same rules"). FINMA, "Supplement to the guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs)", 11 September 2019, <https://www.finma.ch/en/~media/finma/dokumente/dokumentencenter/myfinma/1bewilligung/fintech/wegleitung-stable-coins.pdf>

(fixed redemption claim in a fiat currency: "classification as a deposit under banking law is indicated"; basket with price-dependent redemption claim: "a collective investment scheme is probable"; mere ownership right: "generally does not qualify as a security"; contractual claim on "bank precious metals": deposit "probable"; other commodities: security "and possibly ... a derivative"). ↩

2. FINMA, media release of 11 September 2019 (above) (enquiry by the Libra Association, Geneva; payment system licence under FMIA; AML; reserve risks and returns "borne entirely by the Libra Association"). On the renaming and the end of the project, Wikipedia (used as a last resort), "Diem (digital currency)", [https://en.wikipedia.org/wiki/Diem\\_\(digital\\_currency\)](https://en.wikipedia.org/wiki/Diem_(digital_currency)) (renamed Diem in December 2020; in January 2022 the Diem Association wound down and its assets were sold to Silvergate Capital for a reported USD 200 million). ↩
3. FINMA, Enforcement case report 2019-15, <https://www.finma.ch/it/documentazione/rendicontazione-in-materia-di-enforcement/kasuistik/2019-15/> (ruling of 15 March 2019; about 37,000 investors; more than CHF 90 million; public deposits without licence, Art. 1 para. 2 BankA; Federal Administrative Court B-2237/2019, decision of 2 March 2021 not to hear the appeal; media release of 27 March 2019). ↩
4. FINMA, media release "FINMA ascertains illegal activity by envion AG", 27 March 2019, <https://www.finma.ch/en/news/2019/03/20190327---mm---envion/> (at least 37,000 investors; more than CHF 90 million; EVN tokens; payments in US dollars, ether and bitcoin; bankruptcy opened by the Cantonal Court of Zug in March 2019). The case report 2019-15 (above) links to this release. ↩

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