

# Initial Coin Offering

A Legal Work Plan





## INTRODUCTION

Switzerland is currently in the midst of the global crypto-finance boom and Swiss-related Initial Coin Offerings («ICOs») are attracting worldwide attention. The high volume of ICOs held in Switzerland (as illustrated by the graphs below) suggests a fintech-friendly legal environment. Switzerland is an attractive jurisdiction for innovators to conduct an ICO.

However, ICO founders, issuers and operators as well as banks that offer services in connection with ICOs are well-advised to thoroughly check each ICO project in advance for compliance with financial market and securities regulations as well as the respective tax implications resulting from such an endeavor.

In this context, this publication presents a general step plan detailing in a chronological order the envisaged legal work relating to the implementation of an ICO project.

We estimate the realistic time horizon for a legally compliant ICO to be ranging between 9 and 12 months given that an ICO regularly challenges different legal disciplines. This includes corporate and contractual law with regard to the set-up of the token issuer, the fund flow and the legal establishment of the token itself as well as regulatory and tax law with regard to the issuance and trading of tokens.

Baker McKenzie Zurich offers its clients legal services anticipating a multitude of legal challenges in a complex environment. Our interdisciplinary professionals work with the support of an international project management team in a cost-efficient manner.

In addition to traditional settlement methods, we also offer innovative fee models that reduce the entrepreneurial risk for our clients.

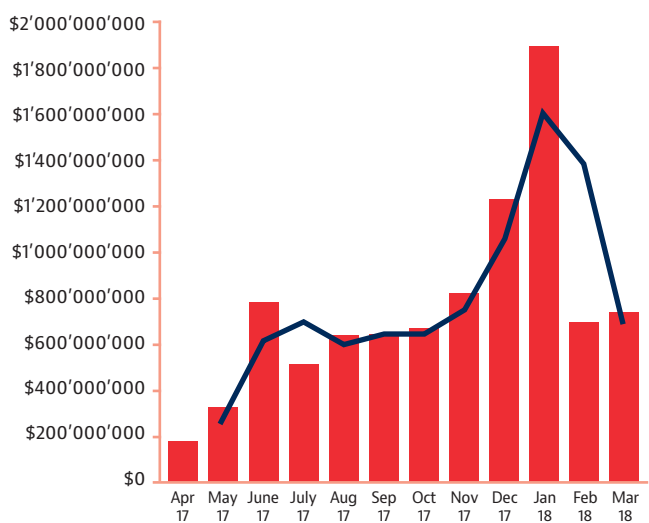


### All time ICO volume by country



Source: icowatchlist.com/statistics (as of June 2018)

### Global ICO volume per month



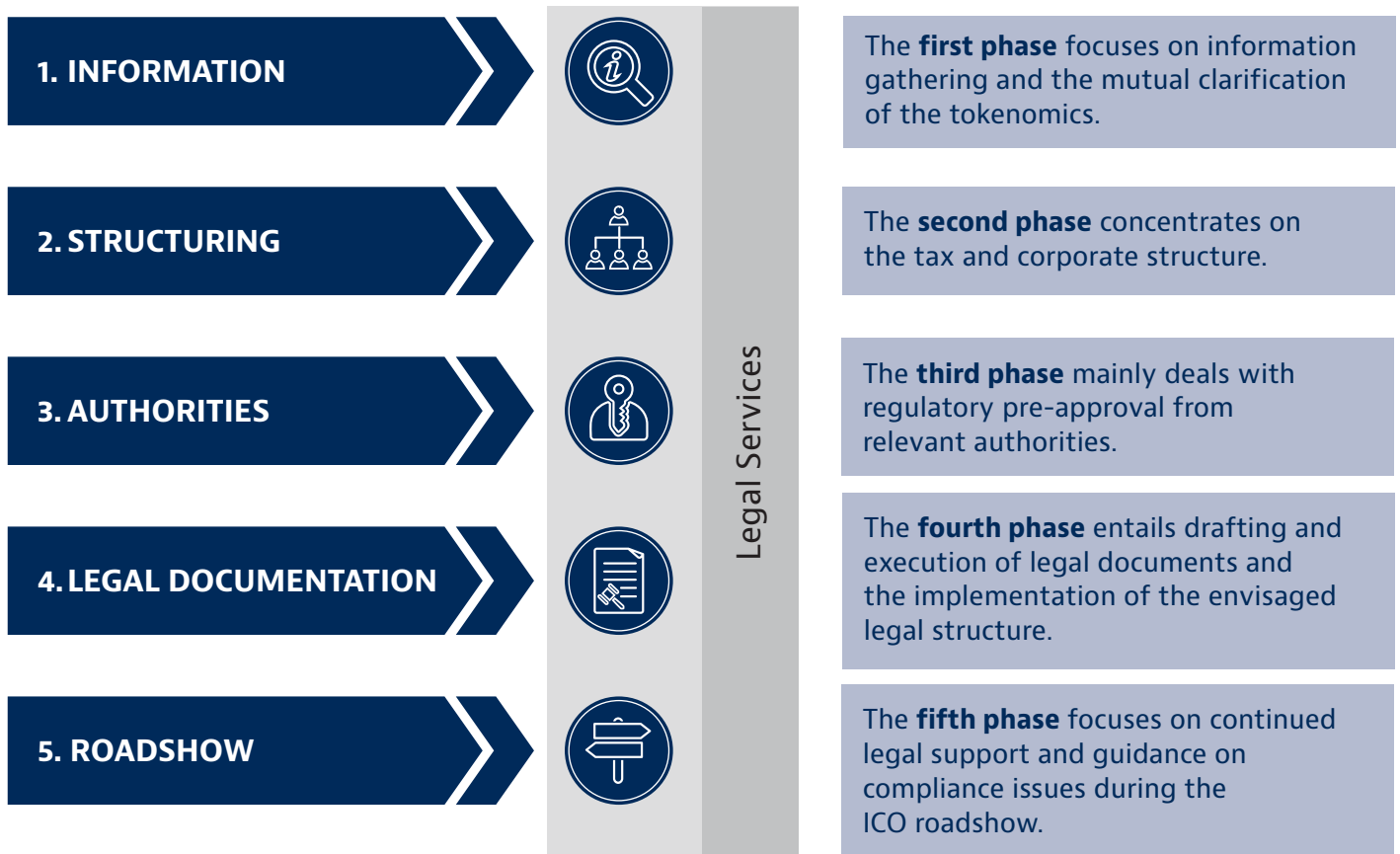
Source: www.coinist.io (as of June 2018)

# OVERVIEW

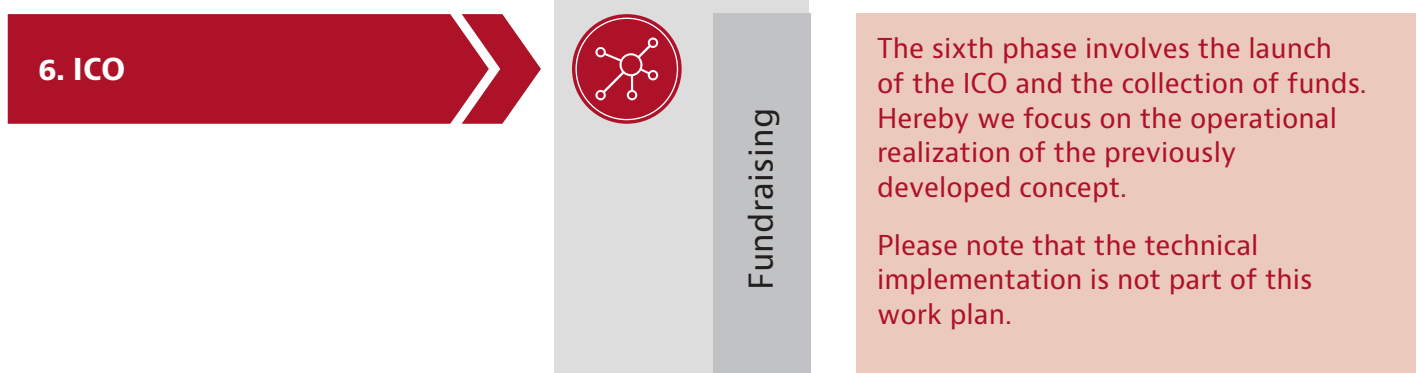
This publication presents a work plan describing in a chronological order the legal work typically required in connection with ICOs and illustrates the usual work products to be developed in this context.

The work plan is divided into the following **six phases**:

## 7-9 months




## 2-3 months



# 1

## Information

### Legal Focus

| No. |   | Steps             | Description   |
|-----|---|-------------------|---|
| 1.1 |  | Questionnaire     | Initial description of ICO project and involved parties         |
| 1.2 |  | Kick-off          | Clarification of ICO project                                    |
| 1.3 |  | Cost estimate     | Setting out the cost framework                                  |
| 1.4 |  | Engagement letter | Defining the scope of work and the conditions of our engagement |



**Duration:**  
2-3 weeks

#### Work Products



Engagement letter



Slide deck on project summary

The main focus of the **first phase** lies on the clarification and specification of the planned ICO project. It is essential to understand the business case, the underlying technology, and the tokenomics of the ICO project in order to be able to identify the initial red flags. This will allow the design of a legal structure fitting the needs of the project from the start. As a general rule, it is essential to identify the following:

### General Information



Identification of legal entities and persons involved (founder, token issuer, token seller, trading participants): name, address, email, website



Name of token



Target ICO market participants (geographical distribution of investors)



Cryptocurrencies (or legal tender) to finance ICO

### Business Case



Determination of business model (platform, project financing, cryptocurrency, investment vehicle, altruistic vs. profit-oriented)



Key features of service



Which market participants (investors) does the ICO target?



Restrictions relating to investors

### Underlying Technology



New or existing technologies used



Technology Partner

## Type of Token

There is no generally recognized classification of tokens. The Swiss Financial Market Supervisory Authority FINMA has determined the following categorization based on the underlying economic function of a token:



**Payment Token** – used as **means of payment** (money, value transfer).



**Utility Token** – provide **access** to a digital application or service on a blockchain-based infrastructure.



**Asset Token** – **represent assets** such as ownership in physical assets, shares in companies or claims. Asset token enable effects, including tangible assets, to be traded on the blockchain.



**Hybrid Token** – combine more than one of the aforementioned token types due to a combination of their feature.

## Areas of legal focus



Jurisdiction and applicable law



KYC process



Acceptance of public deposits



Liability questions/indemnification strategies/insurance options







Withholding tax issues, transfer pricing, applicable double taxation agreement («DBA»)



US securities law

# 2 Structuring

## Legal Focus

| No.   | Steps                        | Description   |
|---|------------------------------|---|
| 2.1  | Corporate/Contract           | Design legal structure  |
| 2.2  | Tax                          | Determine tax residence   |
| 2.3  | Regulatory                   | Assessment of applicable regulations and identification of duties |
| 2.4  | Intellectual Property («IP») | Allocation and registration of IP                                 |



**Duration:**  
1-2 months

### Work Products



Slide deck on proposed legal structure and legal steps



Transfer price study, if deemed necessary

The main focus of the **second phase** lies on the legal structuring of the planned ICO project and the issuing entity. A clear legal structure is the essential backbone of every successful ICO. We qualify an ICO as successful if the envisaged funds can be collected, these collected funds can be used as required and none of the ICO participant, in particular the founders, are facing the threat of civil and criminal sanctions, especially in the U.S.

## 2.1 Corporate/Contract

The legal entity type of the token issuer has to be determined carefully. In the past, the Swiss foundation was regularly used. The foundation has certain advantages, but also challenges regarding profit-oriented projects when it comes to the use of funds. Regularly, the remuneration of the ICO participants providing services to the foundation and the consideration paid by the latter for IP raises various legal and tax challenges. In such cases, different legal entities connected by a tax streamlined contractual network might provide a suitable solution. However, traditional legal entity types like the limited liability company and the company limited by shares offer more flexibility and simpler procedures for the acceptance of new shareholders and the transfer of ownership.

## 2.2 Tax

The issuance of a token may trigger various tax consequences. Depending on the token type, the main focus is on profit tax, value added tax and possibly withholding tax. The tax consequences mainly depend on the tax residence of the token issuer and other relevant ICO participants.

## 2.3 Regulatory

Whether an ICO falls within the scope of Swiss financial market regulation has to be determined in each individual case, as the answer to this question depends on the functionalities and rights of the offered token.

It can be essential to obtain a «no enforcement action letter» from the competent market supervisory authorities to prevent regulatory enforcement procedures that may be initiated a few years after the ICO project.




## 2.4 Intellectual Property («IP»)

The early patenting or copyright treatment of IP enables effective protection against unjustified interference by third parties and facilitates its recognition on the balance sheet.

As part of an initial analysis, current and future IP is evaluated for their protection worthiness and, if necessary, appropriate registration procedures are initiated.

# 3 Authorities

## Legal Focus

| No.   | Steps               | Description                         |
|---|---------------------|-------------------------------------|
| 3.1  | FINMA               | «No enforcement action letter»      |
| 3.2  | Tax Authorities     | Federal and Cantonal tax rulings    |
| 3.3  | Commercial Registry | Pre-approval of corporate documents |

The main focus of the **third phase** lies on clearance of the entire legal implementation of the ICO by the competent Swiss authorities. Of course, depending on the ICO structure, foreign authorities might also have to be involved. It is often vital to get preapproval(s)/«no enforcement action letter» from authorities before implementing an ICO.

The two relevant authorities relating to ICOs performed out of Switzerland are

the Swiss Financial Market Supervisory Authority and the tax authorities. In addition, we recommend to get pre-approval by the competent Swiss commercial registry before setting up any legal entities.

While FINMA will determine which regulatory framework is applicable to the token, the tax authorities will assess the tax consequences of the token issuance, the use of the collected funds and of the transfer of tokens.



**Duration:**  
2-3 months

### Work Products



FINMA «no enforcement action letter»






Tax ruling(s)



Pre-approval(s) of commercial registry

# 4 Legal Documentation

## Legal Focus

| No.   | Steps                  | Description   |
|---|------------------------|---|
| 4.1  | Corporate/<br>Contract | Due diligence with focus on preexisting relevant legal entities and contracts; draft legal documents; prepare/review white paper (prospectus in case of securities offerings) |
| 4.2  | Regulatory             | Due diligence with focus on preexisting legal entities; coordination of KYC obligations; prepare/review white paper (prospectus in case of securities offerings)              |
| 4.3  | IP                     | Due diligence with focus on existing IP rights; prepare documentation for registration/transfer of IP   |



**Duration:**  
2-3 months

### Work Products



DD Report



White paper or prospectus



Legal documentation




The **forth phase** deals with the preparation of the legal structure and its implementation after all rulings and «no enforcement action letters» have been received.

Of course, it is possible to start with the drafting of the relevant legal documents like corporate deeds, contracts and the white paper or prospectus (in case of securities offering) before the filing of the tax ruling(s) and the pre-approval request(s) addressed to the competent commercial registry in order to meet the proposed timing.

However, the execution and publication of such documentation is regularly subject to the approval of the competent authorities. Otherwise, there might be a risk that the ICO project is jeopardized.

# 5 Roadshow

## Legal Focus

| No.   | Steps                  | Description   |
|---|------------------------|---|
| 5.1  | Corporate/<br>Contract | Additional general legal advice, in particular in response to investors questions                       |
| 5.2  | Regulatory             | Supervision of road show documentation  |
| 5.3  | IP                     | Additional advice on registration and licensing of IP, in particular in response to investors questions |



Duration:  
2 months

### Work Products





Continued legal advice

When issuing an asset token incorrect statements regarding future sales and earnings of the token issuer during a roadshow may form a basis for liability. In the context of securities offerings, the white paper/full-fledged prospectus published is the cornerstone of investor communication and expectation management.

During the **fifth phase** we therefore offer the possibility of subjecting all communication with investors to a legal review in order to avoid statements which could possibly give rise to liability.

# 6 Authorities

## Legal Focus

| No.   | Steps                  | Description                    |
|---|------------------------|--------------------------------|
| 6.1  | Corporate/<br>Contract | Signing of remaining documents |
| 5.3  | IP                     | Completion of registrations    |



Duration:  
2-3 months

### Work Products



Continued legal advice

After successful completion of the structuring, the **sixth and final phase** constitutes the effective performance of the ICO through which tokens are issued for the agreed consideration.

Based on the previous preparatory work, the collected funds will be immediately available for operational usage.

Baker McKenzie's diverse and international team remains at the disposition should any post-ICO legal questions arise.



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