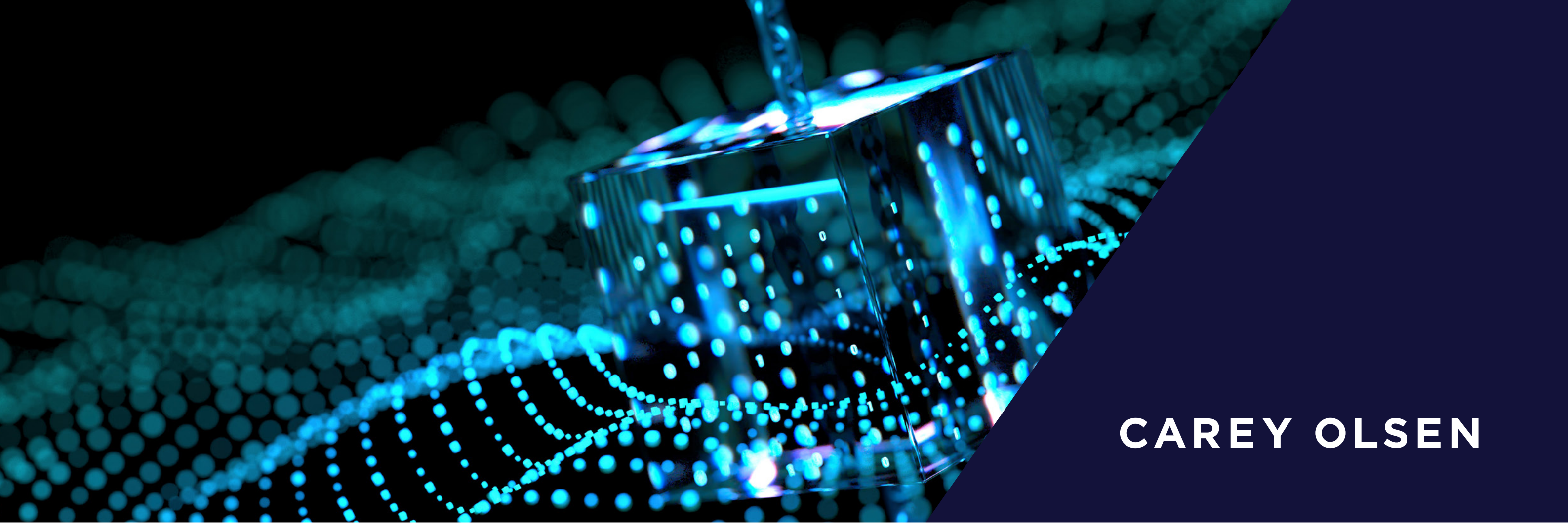

Jersey publishes new guidance on the tokenisation of real world assets (“RWAs”)

Service area / Investment Funds, Regulatory
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The Jersey Financial Services Commission (“**JFSC**”) has published pragmatic new guidance on the tokenisation of real world assets (**“RWAs”**) aimed at Jersey issuers, to promote Jersey’s competitiveness as an international finance centre in the digital assets space.

The guidance aims to clarify the process for issuing a digital representation of a real world asset on a blockchain by a Jersey issuer, and is designed to ensure a proportionate regulatory framework that upholds investor protection and market integrity, whilst supporting industry by clarifying the JFSC’s regulatory expectations.

What is tokenisation?

Tokenisation is the process of issuing a digital representation of an asset, typically on a blockchain, and its benefits include allowing investors to own and sell fractions of an asset which may otherwise be illiquid and/or financially unattainable for such investors to own outright. Examples of the types of assets which may be tokenised include real estate, fine art, commodities, bonds, interests in funds, other types of securities and intellectual property rights.

The JFSC’s treatment of stablecoins as being the tokenisation of fiat currencies

Stablecoins (which are tokens whose value is tied to a fiat currency such as one US dollar or one Euro) have previously been treated by the JFSC as cryptocurrencies but will now be viewed as tokenisations of RWAs. The JFSC expects stablecoins to be fully asset-backed by low risk assets such as money market funds, rather than algorithmically based.

The JFSC will now require the following information to be included in any application to launch a stablecoin (noting that this is not an exhaustive list of the information they may require):

- details of the assets being held as collateral, for example cash and cash equivalents, and clear information on the short-term liquidity of those assets;
- collateral custody arrangements, for example whether there are multiple custodians to reduce any concentration risk;
- information on who may directly purchase the stablecoins from the issuer, for example, authorised participants, and who can redeem their stablecoins for fiat; currencies and
- details of any de minimis threshold for issuance and/or redemption of the stablecoins.

Requirements applicable to issuers

Issuers must meet specific requirements, including being companies or limited liability companies incorporated in Jersey, complying with AML/CFT standards, and arranging independent verification of underlying RWAs. Issuers should also be mindful that the guidance is an overlay to the existing Jersey regulatory regime so, for example, if units in a Jersey fund will be tokenised, the usual Jersey funds regime will apply to that fund before its units are able to be tokenised.

The JFSC will consider each application on a ‘case by case’ basis with regard to the type(s) of assets being tokenised but will expect all issuers to:

- be incorporated as a Jersey company or Jersey limited liability company;
- be administered through a trust and company service

provider licensed by the JFSC under the Financial Services (Jersey) Law 1998, as amended, to carry out "trust company business" ("**TCB**"), and that TCB must conduct due diligence on the issuer to satisfy itself regarding matters ranging from the issuer's honesty and integrity to its financial resources and AML/CFT and security measures;

- appoint and maintain a Jersey-resident director on the governing body of the issuer, who is a natural person and a principal person of the TCB appointed by the issuer;
- receive consent under the Control of Borrowing (Jersey) Order 1958 ("**COBO**") from the JFSC before it undertakes the token issuance;
- apply all relevant AML/CFT requirements to persons that either purchase tokens from, or sell tokens back to, the issuer of those tokens and perform enhanced measures where higher AML/CFT risks are identified, to effectively manage and mitigate those higher risks;
- develop and implement policies, procedures and controls including those in relation to conduct, customer due diligence and transaction monitoring, screening, suspicious activity reporting and record keeping;
- monitor the implementation of those policies, procedures and controls, and enhance them if necessary;
- arrange for all smart contracts (deployed in the year) to be audited and the results to be made public;
- independently verify underlying assets by a qualified third party and publish those results within three months of the end of the issuer's financial year end;
- prepare and submit an information memorandum (which may be in the form of a white paper) to the JFSC, which complies with certain content requirements for a prospectus issued by a Jersey company;
- ensure that any marketing material (including the information memorandum) is clear, fair and not misleading; and
- consider the intended purpose of the tokens against activities detailed within Table 1 and Table 2 of the JFSC's Sound Business Practice Policy, under which involvement in virtual assets is considered to be a "sensitive activity" requiring certain AML/CFT obligations to be imposed upon the issuer.

The JFSC's prior consent will be required for any change of TCB or Jersey resident director.

Disclosures and risk warnings

Any entity which sells tokenised RWAs may be obliged to bring risk warnings to the attention of any direct customer. These risk warnings will to an extent be bespoke, based on the product offering, and may include disclosures relating to the underlying technology and the token's price difference compared to the price of the underlying asset.

Furthermore, if the rights of the token differ to the rights of holding the underlying asset, this should be clearly disclosed to the buyer. For example, the holding of a tokenised equity share may not include the same voting rights and qualification for dividends as holding the untokenised equity share. In this case, the applicant must detail who has received those rights and how those rights are being exercised (e.g. who is voting/how will distributions be dealt with?).

Ongoing requirements which will apply to the tokenised RWA

The following requirements are expected to apply in all cases, and may be included as conditions to the COBO consent issued by the JFSC:

- underlying assets are to be independently verified by an appropriately qualified third party at least annually and the results of this validation made available to the public (this validation should confirm that the tokens are 100% collateralised and ring-fenced);
- underlying RWAs are to be held by a professional custodian with accountability in an equivalent jurisdiction;
- assets are to be ring-fenced and not lent out for additional yield unless expressly agreed by the JFSC, for example, acceptable circumstances may include a stablecoin issuer holding highly liquid cash equivalents;
- appropriate disclosures are to be displayed publicly by the issuer including the performance of the token against NAV;
- where the issuer or custodian ceases business activity, they should provide details of how the underlying assets will be distributed (or otherwise realised) to the holders of the tokens;
- if relevant, details should be provided on how any income, dividends or other distributions are allocated to the token holders, for example whether this is executed through a smart contract or manually to those wallets holding the token;
- details should be provided of any additional (or reduced) rights that the holder of the token is granted, for example, voting;
- there shall be no change in counterparties of the issuer without prior approval of the JFSC; and
- there should be documentation of the key risks and mitigants of those risks, including considerations around which blockchain the token is to be issued on and the liquidity of the tokens in secondary markets.

The issuer's board of directors must advise the JFSC promptly if the issuer defaults on any token issued or is unable to redeem tokens within a reasonable period (for example, as the token is held by someone who cannot satisfy the necessary AML/CFT requirements).

Summary

The new guidance sets out clear practical measures to be taken by issuers depending upon factors such as the nature of the RWAs. The standardisation of the application process and requirements applicable to Jersey issuers reflect Jersey's growing maturity in this asset class and the pragmatism of the Jersey regulator in welcoming new fintech businesses to conduct their activities in the island.

Continued

A copy of the full guidance may be found at Initial coin/token offerings and tokenisation of real world assets – Jersey Financial Services Commission (jerseyfsc.org).

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