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## MEMORANDUM

05 August 2018

### VIA EMAIL

**To:** GVE Ltd  
**From:** Latham & Watkins  
**File no:** 062198-0001  
**Copies to:** Koji Fusa  
**Subject:** Characterisation of the EXC Token and Regulatory Implications for the EXC Token Offering and Launch of the EXC Token Trading Platform in the UK

## 1. BACKGROUND

- 1.1 The contents of this Memorandum are subject to the assumptions and qualifications set out at Annex I.
- 1.2 We understand that GVE Ltd (**GVE**), Global Monetary Foundation (**GMF**) and Excor Ltd (**Excor**) (together the **Group**) intend to establish a platform (the **EXC Platform**) to facilitate the transfer of the EXC Token (**Token**) as a means of digital value transfer. The intention is that the Token and the EXC Platform will be utilised by central banks (and other market participants) to facilitate transfers in Tokens on the EXC Platform. In addition to the EXC Platform, we understand that Excor is considering establishing an electronic trading platform in the UK to facilitate the secondary trading of the Token.
- 1.3 We understand that GMF will issue and loan (not yet subscribed for) Tokens to GVE. GVE will in turn loan a proportion of these Tokens to Excor, retaining a proportion of Tokens to fund certain development costs. Excor will sell the borrowed Tokens to purchasers (**Purchasers**). The sales will take place by way of a private token offering or a series of private token offerings (together the **Private Token Offering**), prior to an eventual public token offering of Tokens (**Public Token Offering**) (together the **Token Offerings**).

### **The Token**

- 1.4 You have told us that:
- (a) the sole purpose of the Token is to function as a means of digital value transfer between users of the EXC Platform;
  - (b) the Token does not entitle the Purchasers/holders of the Token to a share in the Group's profits (such as, but not limited to, payment of dividends), or to exercise voting rights in relation to the Group;

- (c) the Token does not entitle its Purchasers/holders to any contractual right to be repaid the purchase price of the Tokens;
- (d) the Token does not represent any other type of claim on the Group for return of any monetary or non-monetary value;
- (e) there is no optionality granted to Purchasers to choose whether or not to take up their Token allocations once they have initially subscribed;
- (f) the Token is not pegged to the value of any fiat currency or commodity; and
- (g) there is no right of assignment that would permit anyone other than the Purchaser of the Token to take delivery of the Token on subscription.

1.5 Simply put, participation in a Private Token Offering or Public Token Offering by Purchasers involves Purchasers agreeing to purchase an amount of Tokens to be received in exchange for their payment of the required subscription amounts.

#### **The Token trading platform**

1.6 You have told us that:

- (a) Excor intends to establish and operate an electronic trading platform in the UK (the “**Trading Platform**”). We understand that the Trading Platform will facilitate the trading of the Token between users of the Trading Platform;
- (b) the Trading Platform will only facilitate transactions for Tokens and only in fiat currency. The Trading platform will not facilitate transactions in any other cryptocurrency or instrument, for example tokenised securities, commodities, other assets or derivatives (users are only able to trade in the Token);
- (c) you have told us that the Trading Platform will operate wallets for users of the Trading Platform to hold their Tokens;
- (d) the Trading Platform will not operate any matching engine functionality (buyers must manually select sell orders in their own discretion and sellers must manually select buy orders in their own discretion);
- (e) Excor will act as principal in relation to all Token trades on the Trading Platform, becoming the buyer to every Token sale and the seller to every Token purchase. Excor will quote buy and sell prices on the Trading Platform and will be on risk for price movements. The Token from each selling customer’s wallet will be transferred into Excor’s wallet. Excor will only sell Tokens held in its own wallet;
- (f) Excor will treat funds received from Token purchasers as proprietary funds that will be paid into the account of Excor. Purchases of tokens by Excor will be paid for with funds from Excor’s proprietary account;
- (g) Excor will enter into counterparty documentation which appropriately reflects the principal-to-principal nature of the transactions on the Trading Platform; and
- (h) GMF will operate to provide liquidity in the trading of the Token by buying and selling Tokens on the Trading Platform in accordance with a liquidity provision technical paper made publicly available for potential purchasers.

## 2. EXECUTIVE SUMMARY

2.1 Based on the information you have provided to us and which is summarised above in section 1 together with the assumptions and qualifications at Annex I, we consider that:

- (a) neither the Tokens nor the issuance and sale of the Tokens to Purchasers by Excor pursuant to the Token Offerings are or involve specified investments subject to the UK regime;
- (b) the sale of the Tokens to Purchasers by Excor pursuant to the Token Offerings will not involve Excor engaging in a specified activity subject to the UK regime;
- (c) the Tokens will not constitute transferable securities for the purposes of the UK prospectus requirements;
- (d) marketing of the Token Offerings by the Group will not constitute a financial promotion under the UK regime;
- (e) should the Trading Platform only facilitate trading in the Token (which is not a specified investment), Excor will not need to be licenced as an operator of a trading facility under the UK regime because these types of regulated activity only fall within the regulatory perimeter if carried on in relation to a specified investment; and
- (f) it is arguable that the Company will not be one of the types of entity caught by the UK anti-money laundering regime in relation to the Token Offerings. However, there is some uncertainty for the reasons set out below at section 4. Accordingly, we would recommend that the Company does perform AML/KYC on the Purchasers of Tokens and users of the Trading Platform despite the arguments in favour of the UK anti-money laundering regime not applying to the Token Offerings and not currently applying to cryptocurrency exchanges. In practice, it may be beneficial for the Company to perform AML/KYC on the Purchasers of Tokens and users of the Trading Platform given that its regulated service providers (such as banks) will need the Company to explain its source of funding during the onboarding process. This will be difficult to achieve if the Company does not perform AML/KYC on the Purchasers and users of the Trading Platform. Due to forthcoming changes to the EU's anti-money laundering regulations, the Trading Platform will very likely be brought within scope of the AML/KYC requirements of the UK regime by January 2020.

As a result, in our view, the Group's participation in and completion of the Token Offerings and operation of the Trading Platform will not involve the performance of a licensable activity by the Group, will not require an approved prospectus and will not be subject to the UK financial promotions regime.

## 3. UK LEGAL ANALYSIS

### Background to the regulatory regime

- 3.1 The Financial Services and Markets Act 2000 (**FSMA**) provides that no person may carry on a regulated activity in the UK unless that person is authorised or exempt (this is referred to as the 'general prohibition'). A regulated activity is simply defined as an activity of a 'specified kind' which relates to an investment of a 'specified kind' (a 'specified investment') or is carried on in relation to property of any kind. For this purpose, 'specified' means specified by the Treasury by statutory instrument.
- 3.2 The relevant statutory instrument is the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (**RAO**). The order identifies specified activities as including activities such as promoting, advising on, managing, arranging deals in, or dealing in, investments.

- 3.3 Although the Treasury is empowered to specify any assets as investments, the RAO specifies shares, bonds and other debt instruments, government and public securities, warrants and tradeable certificates for any of the foregoing, mortgages, options and futures, contracts for differences, units in a collective investment scheme, and other similar financial instruments.
- 3.4 The statutory consequences of a breach of the general prohibition are severe:
- (a) the infringer commits a criminal offence;
  - (b) any contract made in the course of carrying on the relevant activity is unenforceable; and
  - (c) there are provisions for compensation and restitution in favour of the other party.

**Analysis of the activities undertaken in relation to the Token Offerings and the Trading Platform**

- 3.5 In order to determine whether the issuance of the Tokens pursuant to the Token Offerings will constitute a regulated activity under the UK regime, it is therefore sufficient to consider (i) whether the Token Offerings will involve specified investments (and in particular whether the Tokens to be issued pursuant to the Token Offerings will constitute specified investments), and (ii) whether the issuance of the Tokens pursuant to the Token Offerings will fall into any of the other various categories of activities which are specified without reference to specified investments.
- 3.6 The Token does not give the holder any rights. The Token is simply a digital representation of value that is comprised of demand and supply for the Token. In our view, the Tokens and the Token Offerings do not involve specified investments and the issuance of the Tokens does not otherwise constitute a specified activity. Accordingly, in our view, the issuance of the Tokens is not a regulated activity, and the Group will not trigger licensing and other consequential regulatory requirements by virtue of GMF's issuance of the Tokens or Excor's sale of the Tokens to Purchasers pursuant to the Token Offerings, provided that the Token is (and remains) structured in line with this Memorandum.
- 3.7 In order to determine whether the operation of the Trading Platform by Excor will constitute a regulated activity under the UK regime, it is sufficient to consider (i) whether the Token to be traded on the Trading Platform will constitute a specified investment, and (ii) whether the operation of the Trading Platform itself will fall into any of the various categories of activities which are specified.
- 3.8 You have told us that the Trading Platform will only facilitate the trading of the Token, which is not a specified investment. To the extent that the Trading Platform was to facilitate the trading of specified investments which constitute MiFID<sup>1</sup> financial instruments (such as tokenised shares, bonds and derivatives), it would likely mean that Excor, as operator of the Trading Platform, would be carrying on a regulated (and licensable) activity of operating a trading facility.
- 3.9 However, if the Trading Platform can ensure that it only facilitates trading in the Token (as described in this Memorandum), Excor will not need to be licenced as a trading facility operator.
- 3.10 It should be noted that even if Excor does not fall within the scope of the UK licensing requirements, Excor could fall within the licensing requirements of other jurisdictions if Excor markets the Platform to customers in other jurisdictions.

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<sup>1</sup> Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU

### Payment services

- 3.11 To the extent that the Trading Platform was to facilitate the trading of stable coins (the value of which are tied to fiat currency), the Trading Platform operator would likely be carrying on regulated payment services, thereby requiring a licence under the UK regime. However, as long as the value of the Token is not tied to fiat currency (and remains so), the Token is not a stable coin nor electronic money under the UK regime. As the Token is the only token traded on the Trading Platform, no regulated payment services are being undertaken by Excor in this regard.
- 3.12 However, the moving of purchaser's fiat funds by Excor (as operator of the Trading Platform), to the accounts of sellers, would be at risk of being characterised as a regulated payment service. The FCA considers that when you transfer funds from or to your clients, enabling them to pay or receive payment by way, for example, of direct debit, payment card, electronic cheque or credit transfer, you will be executing payment transactions, which is a regulated payment service and which requires a licence. However, you have told us that you will not facilitate payments between buyers and sellers of Tokens, as Excor is acting as principal and will be the buyer to every seller of Tokens, and the seller to every buyer of Tokens and as such, in our view, Excor will not be conducting regulated payment services.

### Prospectus requirements

- 3.13 FSMA prohibits the offering of transferable securities<sup>2</sup> to the public in the UK unless an approved prospectus has been made available to the public prior to the offer, or an exemption applies. FSMA also prohibits the request to admit transferable securities (other than a limited number of exempted transferable securities) to trading on a regulated market situated or operating in the UK unless an approved prospectus has been made available to the public before the request is made.
- 3.14 For the purposes of our analysis it is not necessary to independently consider whether the Tokens will constitute transferable securities provided that they do not constitute specified investments. Accordingly, given our conclusion above that the Tokens will not constitute specified investments, it is also our view that the Tokens will not constitute transferable securities. Therefore, in our view, the UK prospectus requirements will not apply to the Token Offerings.

### Financial promotions regime

- 3.15 The UK regime also contains a restriction on financial promotions, according to which a person who is not authorised must not, in the course of business, communicate an invitation or inducement to engage in investment activity.
- 3.16 The term "*engaging in investment activity*" is in turn defined in FSMA by reference to various "*controlled activities*" and "*controlled investments*". Provided that our analysis does not rely on any exclusions in order to reach the view that the Tokens and the Token Offerings do not

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<sup>2</sup> In our view it would be technically possible to query whether the MiFID notion of transferable security is a subset of the RAO notion of specified investment, however in practice we think there is very little risk of any such divergence arising in practice. The technical possibility of divergence arises because the notions have distinct historical origins in different regimes, and although the UK legislative framework has been updated to align with MiFID there is still therefore the technical possibility that various categories of UK specified investment do not themselves precisely map on to the corresponding MiFID concepts (and in particular, although the UK regime does contain a legislative mechanism which is designed to restrict the possibility of divergence, known as the "MiFID Override", the precise way in which the MiFID Override operates does not guarantee a one-to-one correspondence between European and UK regulatory concepts). In practice however, we think this possibility is highly unlikely – we are not, for example, aware of any financial instruments which fall under the MiFID notion of transferable security, but which would not be categorised as one or other kind of specified investment under the UK regime.

involve specified investments or activities, it will follow that the Tokens and the Token Offerings do not involve controlled investments or activities for the purposes of the financial promotions regime. The analysis set out in this Memorandum does not rely on any such exclusions, and so in our view the Group will not violate the prohibition on financial promotion by promoting the Token Offerings or the Trading Platform in the UK.

#### 4. UK ANTI-MONEY LAUNDERING REGIME

4.1 The UK anti-money laundering regime is set out in the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the “**MLRs 2017**”). The MLRs 2017 apply the following types of institution, entity or person:

- (a) credit institutions;
- (b) financial institutions;
- (c) auditors, insolvency practitioners, external accountants and tax advisers;
- (d) independent legal professionals;
- (e) trust or company service providers;
- (f) estate agents;
- (g) casinos; and
- (h) high value dealers<sup>3</sup>.

4.2 Excor, as the Trading Platform operator, will not fall within any of the types of institution, entity or person listed in paragraphs (a)-(g) above.

4.3 “*High value dealers*” are defined in Article 14(1)(a) of the MLRs 2017 to mean a firm or sole trader who by way of business trades in goods (including an auctioneer dealing in goods), when the trader makes or receives, in respect of any transaction, a payment or payments in cash of at least 10,000 euros in total, whether the transaction is executed in a single operation or in several operations which appear to be linked.

4.4 There is no definition of “*goods*” in the MLRs 2017 and, therefore, it is not clear whether cryptocurrency tokens would fall within the definition of goods for the purposes of the MLRs 2017. In relation to MiFID, the FCA has clarified that in PERG 13.4 Q33<sup>4</sup> (of the FCA Handbook) “*currencies or rights in real estate, or that are entirely intangible*” are not “*goods*”, and therefore will not constitute commodities. However, it is not clear that the same interpretation would be adopted in relation to the MLRs 2017 and there is no guidance on this point.

4.5 In addition, “*cash*” is not defined. It is arguable that the reference to cash relates to banknotes and coins. However, the term cash is often given a broader definition by UK regulation to distinguish cash transactions (including commercial bank money and electronic money) from credit transactions or physically settled derivatives. Guidance is provided by the UK government on its webpage for “*Money laundering supervision for high value dealers*”, which states that dealers who are only ever paid large amounts by credit card, debit card or cheque do not need to register as high-value dealers<sup>5</sup>. This suggests that the narrower definition of

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<sup>3</sup> Article 8, MLRs 2017.

<sup>4</sup> <https://www.handbook.fca.org.uk/handbook/PERG/13/4.html>

<sup>5</sup> <https://www.gov.uk/guidance/money-laundering-regulations-high-value-dealer-registration>

cash (as banknotes and coins) should be adopted. However, it is not clear how definitive these guidelines are and whether a court would take the same view.

- 4.6 Accordingly, there are arguments that the Trading Platform should currently fall outside the scope of the MLRs 2017.
- 4.7 However, we note that the EU's fifth Money Laundering Directive ("**MLD5**") will come into force by 10 January 2020 and will force changes to the MLRs 2017. MLD5 will require virtual currency exchange platforms and custodian wallet providers to perform due diligence on their customers, including KYC checks. Such entities will also need to be registered for AML purposes. Consequently, these entities will be regulated for AML purposes in the same way as financial services firms (and subject to the same AML regulatory obligations). The Trading Platform will very likely fall within the definition of a virtual currency exchange for these purposes.
- 4.8 Accordingly, Excor should anticipate that the Trading Platform is likely to fall within the scope of the EU/UK AML/KYC requirements by 10 January 2020.

## ANNEX I

For the purposes of this Memorandum, we have made the following assumptions and qualifications:

- 1.1 Our advice is based on the information set out in the draft EXC Whitepaper and discussions with you on the structuring of the Trading Platform. We have only reviewed the draft EXC Whitepaper and have not received any other information regarding the Token, the EXC Platform, the Trading Platform or the Token Offerings either from you or from your advisers.
- 1.2 Our advice is restricted to considering whether:
  - (a) the Tokens constitute a regulated investment or asset in the UK;
  - (b) the issuance of the Tokens to purchasers pursuant to the Token Offerings constitutes a "*regulated activity*" as defined in FSMA, and hence whether the issuance of the Tokens to purchasers pursuant to the Token Offerings may be undertaken by Excor in the UK without triggering licensing requirements;
  - (c) the operation of the Trading Platform constitutes a "*regulated activity*" as defined in FSMA, and hence whether the activities of the Trading Platform may be undertaken by the Excor in the UK without triggering licensing requirements;
  - (d) the Token Offerings will be subject to the UK prospectus regime as set out in s.85 of FSMA;
  - (e) the Group's promotion of the Token Offerings falls within the UK financial promotions regime set out in s.21 FSMA; and
  - (f) the Group will be subject to the UK anti-money laundering regime as set out in the MLRs 2017.
- 1.3 Accordingly, we have not considered issues arising under the UK consumer rights regime, including the Consumer Rights Act 2015 and the Unfair Contract Terms Act 1977. Although there are certain regulatory requirements relating to consumer rights, we note that these issues generally give rise to civil (rather than regulatory or criminal) risks. In addition, we have not at this stage considered the steps for compliance with UK or international financial sanctions-related legislation but we would be happy to advise the Group on the steps it should take to comply with such legislation in advance of the Token Offerings.
- 1.4 We assume that no Group entity is a regulated entity for the purposes of the UK regime.<sup>6</sup>
- 1.5 We are not providing any analysis of the application of the UK regulatory regime to the EXC Platform itself, to any transactions which may be carried out on the EXC Platform or any services performed on the EXC Platform. We would be happy to provide further advice on this issue at the appropriate time post-financing in advance of the EXC Platform becoming operational.
- 1.6 Our advice is limited to the position as at the date of this Memorandum. We note that cryptocurrencies, token offerings and token trading platforms are currently subject to considerable regulatory attention, and it is not possible to rule out future changes to regulatory expectations or to the UK regime which would require us to revisit the analysis set out in this Memorandum. We note that there is a lack of customary practice and understanding in relation to the regulatory position of token offerings, and to our knowledge no judicial decisions have been issued with respect to the regulatory characterisation of the offering, sale

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<sup>6</sup> i.e. that neither GMF, Excor or GVE are an authorised person for the purposes of FSMA s.19; similarly we assume that neither is an exempt person (such as certain kinds of investment exchanges or clearing houses) for the purposes of this provision.



or issuance of tokens or coins issued by a blockchain (or other technology based) platform in exchange for value.

- 1.7 We have not seen the operation of the live Trading Platform and we have not received any other information regarding the Trading Platform.
- 1.8 It should be noted that even if Excor does not fall within the scope of the UK licensing requirements, as operator of the Trading Platform it could fall within the licensing requirements of other jurisdictions if Excor markets the Trading Platform to customers in other jurisdictions.
- 1.9 We assume that the Trading Platform is not a regulated entity for the purposes of the UK regime.<sup>7</sup>
- 1.10 Given the preliminary stage of the Token Offerings and development of the Trading Platform and the requirement for final confirmation of the detailed structure, this Memorandum may need to be updated once the detailed structure is finalised.

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<sup>7</sup> i.e. that neither the Trading Platform or Excor is an authorised person for the purposes of FSMA s.19; similarly we assume that neither the Trading Platform nor Excor is an exempt person (such as certain kinds of investment exchanges or clearing houses) for the purposes of this provision.