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Blockchain

Switzerland: Law & Practice
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Law and Practice

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1. BLOCKCHAIN MARKET AND BUSINESS MODEL OVERVIEW

1.1 Evolution of the Blockchain Market

Over the last 12 to 24 months, the Swiss blockchain ecosystem has grown and matured in terms of both substance and businesses.

According to the latest CV VC Top 50 Report, published by CV VC AG on 28 February 2021, the top 50 blockchain and cryptocurrency companies in Switzerland and Liechtenstein are valued at USD254.9 billion, representing a tenfold increase in value compared to the previous period.

According to the CV VC Top 50 Report, funding of these companies has reached USD3.7 billion in total. The number of blockchain and crypto companies has reached more than 950, and the number of people employed in the blockchain ecosystem has increased to 5,184.

The Canton of Zug is the centre of the so-called Crypto Valley. Other important technological hubs are Zurich, Geneva, Ticino, Vaud, Lucerne and Berne.

The biggest blockchain projects currently being implemented in the Swiss Crypto Valley include Ethereum (USD401 billion), Cardano (USD42.69 billion), Polkadot (USD35 billion), Solana (USD12.69 billion), Aave (USD6.3 billion), Cosmos (USD4.8 billion) and Tezos (USD4.65 billion).

In April 2021, the Swiss Financial Market Supervisory Authority (FINMA) issued a securities firm licence to Taurus SA, which launched its Taurus Digital eXchange (TDX) in May 2021. Over the last 24 months, FINMA has now issued new banking or securities firm licences to three Swiss domiciled blockchain service providers – SEBA Crypto AG (registered in the Canton of Zug), Sygnum AG (registered in the Canton of Zurich) and Taurus SA (registered in the Canton of Geneva). These licensed financial institutions provide digital services related to brokerage, tokenisation, asset management, banking and/or custody as well as decentralised finance (DeFi).

As of May 2021, the blockchain ecosystem is still thriving in Switzerland despite the ongoing COVID-19 pandemic, with many crypto-based Swiss companies or projects handling the crisis well thus far. However, it is uncertain whether multiple blockchain start-ups can obtain sufficient funds or generate sustainable turnover to survive the COVID-19 crisis.

1.2 Business Models

The use cases of blockchain in Switzerland include cryptocurrency exchange platforms, tokenisation platforms, custodial and non-custodial wallet services, hot and cold storage solutions, supply chain and trade finance solutions, and DeFi applications.

For example, in relation to trading in securities and the clearing and settlement of securities operations, the SIX Digital Exchange (SDX) is creating a fully integrated issuance, trading, settlement and custody infrastructure for digital assets. SDX will focus on a business-to-business model and will operate as regulated financial market infrastructure (including functioning as an exchange and a centralised securities depository). SDX became a member of the Enterprise Ethereum Alliance (EEA) in April 2021, and is expected to start its operations in the second half of 2021.

As of May 2021, Switzerland (as well as the global blockchain community) is still awaiting the full implementation of Ethereum's new "proof-of-concept" (Eth 2.0) – ie, the successful transformation of Ethereum's protocol from a proof of work protocol to a fully fledged proof of stake

consensus mechanism (staking platform). Once the transformation is successfully completed, the network's scalability, security and resilience are expected to be improved. In turn, it may be a more reliable underlying protocol for DeFi applications that can be used by any other market participants. In the last half year, however, DeFi products and services based on other blockchains have increasingly edged into the Swiss DeFi market.

1.3 Decentralised Finance Environment

Demand for DeFi products and services has been growing rapidly over the past six months. In particular, licensed institutions such as Sygnum AG, Seba Crypto AG and TDX eXchange have commenced offering (or intend to offer) – for example – stablecoins to execute and settle transactions in cryptoassets, or decentralised investment platforms with staking functionalities and liquidity providing services.

The Swiss regulator has a technology-neutral position that also applies to DeFi products and services, and thus allows market participants to operate in the DeFi ecosystem as long as they comply with Swiss financial market regulation. For such regulatory assessment, FINMA focuses on the project's functionalities (substance-over-form) and applies the principle of "same business, same risks, same rules".

2. REGULATION IN GENERAL

2.1 Regulatory Overview

On 27 November 2019, the Federal Council proposed new rules for digital assets and submitted the dispatch on the draft Federal Act on the Adaptation of Federal Law to Developments in Distributed Ledger Technology (DLT Bill) to the Swiss Parliament, to reflect the technological developments and improve the regulatory framework for distributed ledger technology (DLT).

The DLT Bill entails specific amendments to the Swiss Code of Obligations, the Federal Intermediated Securities Act, the Federal Act on International Private Law, the Federal Debt Enforcement and Bankruptcy Act, the Federal Banking Act, the Federal Financial Institutions Act, the Federal Financial Market Infrastructure Act and the Federal Anti-Money Laundering Act (AMLA). The Swiss Parliament adopted the DLT Bill in September 2020.

On 1 February 2021, the Federal Council partially enacted the DLT Bill – ie, the amendments to the Swiss Code of Obligations, the Federal Intermediated Securities Act and the Federal Act on International Private Law to enable the creation of the so-called ledger-based securities. The remaining provisions of the DLT Bill concerning, inter alia, the amendments to the Swiss banking regulation, financial market infrastructure regulation and the anti-money laundering regulation will enter into force on 1 August 2021.

As of today, neither blockchain technology nor cryptocurrencies are governed by any sector-specific laws or regulation. Hence, existing laws and regulation apply to the new blockchain technology and, respectively, blockchain-based business models. The new rules will not disrupt the application of the current regime, under which several statutes must be taken into consideration.

Consequently, before a blockchain-based business model is implemented or digital assets are marketed, the project owner should be aware that several statutes may apply in Switzerland (in addition to foreign laws). For example, an initial coin offering (ICO) and/or the envisaged business model may trigger licensing requirements pursuant to one or more Swiss financial

market regulations (such as the Banking Act, the Collective Investment Schemes Act, the Financial Services Act, the Financial Institutions Act, the Financial Market Infrastructures Act and/or AMLA).

Initially, FINMA clarified that the existing laws remain applicable to blockchain-based companies or cryptocurrency-related business models, subject to any changes in law or amendments to existing statutes. Going forward, market participants using blockchain technology or cryptocurrency may be subject to one or more laws as the new rules will only partially amend the existing statutes.

2.2 International Standards

In broad terms, Swiss anti-money laundering regulations have implemented the recommendations of the Financial Action Task Force (FATF), particularly with respect to cryptocurrencies or virtual currencies and following the FATF's adoption of the guidance on the application of the risk-based approach to virtual assets (VA) and virtual asset service providers (VASPs).

FINMA published its guidance concerning payments on blockchain in August 2019. The purpose of this guidance is to clarify and inform market participants about the regulatory requirements related to the FATF's "travel rule" that should be complied with by financial intermediaries.

On 7 February 2020, FINMA further proposed to amend its Anti-Money Laundering Ordinance (AMLO-FINMA) to implement a FATF recommendation for dealing with VASPs. Pursuant to the proposal, the threshold for customer identification in cryptocurrency exchange transactions shall be reduced from CHF5,000 to CHF1,000 in accordance with the FATF recommendation. The amendment entered into force on 1 January 2021.

Apart from FATF recommendations and as regards blockchain-based payment systems or stablecoins, FINMA has also made it clear that the regulatory requirements for such payment systems are based on international standards, such as the Principles for Financial Market Infrastructures (PFMI).

2.3 Regulatory Bodies

FINMA is the regulatory body most relevant to businesses or individuals using blockchain technology or operating fintech companies in Switzerland. As supervisor and regulator, FINMA is responsible for protecting investors and creditors. It also ensures that the Swiss financial market functions properly and may therefore publish guidelines, information for individuals or public warnings. In the field of blockchain and fintech, FINMA can be approached for a pre-assessment concerning tokens or business models.

2.4 Self-regulatory Organisations

In Switzerland, there are several self-regulatory organisations (SROs) that may supervise blockchain-based businesses. As a matter of principle, blockchain-based businesses that qualify as financial intermediaries must either be licensed by FINMA – for example as a securities firm, a payment system or a fintech company – or affiliated with an SRO. In the latter case, FINMA may only supervise blockchain-based businesses indirectly via the SRO.

Such an SRO is responsible for monitoring its members' compliance with Swiss anti-money laundering regulation encompassing, inter alia, AMLA and the SRO's rules and regulations.

Apart from these supervisory bodies, various trade groups and associations have mushroomed in the Swiss blockchain ecosystem – eg, the Bitcoin Association Switzerland, the Swiss Blockchain Federation, the Capital Market Technology Association (CMTA) and the Crypto Valley

Association. These associations have no supervisory power but can participate in legal consultation processes and/or may set best practice standards on a non-binding basis. Examples of such standards include the Digital Assets Custody Standard and the AML Standards for Digital Assets (each published by CMTA).

2.5 Judicial Decisions and Litigation

To date, there is no Swiss court decision explicitly interpreting or determining the applicability of Swiss laws to the use of blockchain or cryptocurrencies.

However, the Swiss regulator has clarified that the existing laws – eg, the Swiss financial market laws – are applicable to new technologies as well. In this context, the initiation of enforcement and bankruptcy proceedings vis-à-vis envion AG are noteworthy. The Swiss Cantonal Court of Zug dissolved envion AG based on Article 731b, paragraph 1, number 3 (Defects in the organisation of the company) of the Swiss Code of Obligations, and ordered its liquidation in a decision of 14 November 2018.

The bankruptcy proceedings of envion AG were conducted as ordinary bankruptcy proceedings controlled by the Bankruptcy Office of Zug (in accordance with the Swiss Debt Enforcement and Bankruptcy Act). Accordingly, the creditors were informed with a "call to creditors", which prompted more than 6,000 creditors to register their claims through an internet portal. The creditors submitted more than 57 million tokens to the bankruptcy administration. In broad terms, this procedure shows that the Swiss courts and authorities apply the existing principles of Swiss civil, litigation and bankruptcy law to blockchain-based or cryptocurrency business.

2.6 Enforcement Actions

In 2020, FINMA carried out approximately 100 preliminary investigations in the fintech or crypto

area. However, FINMA noticed a decline in ICOs compared to previous years.

In 2019, as regards secondary market-related financial services in the crypto area, FINMA identified breaches of the Swiss Banking Act and/or the Swiss Stock Exchange Act, for example, by a provider of token trading and custody services and by a provider of money transmitting services. Important examples of enforcement actions to better understand the "regulatory perimeter" in Switzerland are FINMA's actions against envion AG (see **2.5 Judicial Decisions and Litigation**). FINMA concluded the enforcement proceedings against envion AG in March 2019 and found that:

- envion AG unlawfully took deposits from the public on a commercial basis for which it should have obtained a (banking) licence in advance;
- the repayment obligation of envion AG vis-à-vis the token owners who made payments in US dollars, bitcoins and ethereums to receive envion tokens was qualified as taking deposits from the public;
- the conditions for the envion tokens issued in a bond-like form during an ICO were not equal for all investors and the prospectuses did not meet the minimum statutory requirements; and
- there was no internal audit unit as required by law.

Had it not been for the liquidation proceedings, as mentioned in **2.5 Judicial Decisions and Litigation**, FINMA could have also ordered the liquidation of envion AG due to breaches of regulatory laws.

Having said that, FINMA is willing to continue to consistently take action against ICO business models that violate or circumvent supervisory laws, such as the banking, securities or

anti-money laundering regulations. Ultimately, this can lead to the company being liquidated by FINMA.

2.7 Regulatory Sandbox

Swiss blockchain-based businesses that may qualify as banks can make use of the banking sandbox.

In order to benefit from the sandbox exception, the following requirements must be fulfilled:

• the acceptance of deposits must not exceed the maximum amount of CHF1 million (even if such deposits are made by more than 20 depositors), provided that such deposits are not invested by the Swiss company and do not bear interest; and
• depositors must be informed (in writing) in advance that the Swiss company is not subject to FINMA supervision and that the deposits are not covered by the deposit protection scheme.

If these criteria are fulfilled, the deposit-taking activity will not be deemed to be "on a professional basis". There is no other regulatory sandbox in Switzerland.

2.8 Tax Regime

In Switzerland, as of May 2021, neither a digital service tax nor any other specific tax legislation applicable to blockchain-based business models or the use of cryptocurrencies has been or is expected to be introduced.

As a matter of principle, existing tax laws apply to crypto business models and blockchain-based services. For example, transactions with crypto-assets will usually be beyond the scope of Swiss transfer taxes. If, however, an asset-backed token qualifies as a "bond-like" instrument as defined in Swiss tax practice, the trading of such an asset token can trigger Swiss securities transfer tax, should a Swiss securities dealer (as defined in Swiss tax law) be involved as a party or intermediary in the transaction.

The Swiss Federal Tax Administration issued a working paper on 27 August 2019 regarding the treatment of cryptocurrencies and other coins or tokens based on blockchain technology for Swiss income, withholding and stamp tax purposes. For the specific tax treatment, this working paper distinguishes between native/payment tokens, asset(-backed) tokens and utility tokens. While this Swiss tax classification is based on the same principles as the classification for Swiss financial market regulation purposes as outlined in **3.2 Categorisation**, the Swiss tax authorities conduct their own analysis and classification, which is not necessarily in line with that of FINMA. The working paper also clarifies that tokens are generally considered as assets that are subject to net wealth taxes imposed by the Swiss cantons and municipalities. Some cantonal tax authorities have also issued guidelines clarifying the tax treatment of crypto-assets based on the general tax legislation.

The Swiss Federal Tax Administration also amended its relevant guideline for Swiss value added tax (VAT) purposes regarding the treatment of cryptocurrencies and other coins or tokens based on blockchain technology, on 20 October 2020. While the use of payment tokens is treated in the same manner as the use of fiat currency, the transfer of asset tokens and utility tokens is generally considered as a supply for VAT purposes. Trading with payment tokens or asset tokens is generally exempt from VAT. By contrast, the transfer of utility tokens is considered a taxable supply for VAT purposes, resulting in Swiss VAT if the place of supply is in Switzerland and no specific exemption applies.

The same principles apply for ICOs: the VAT treatment of an issuance of crypto-assets

depends on the characterisation thereof. The issuance of payment tokens is not considered a supply, the issuance of asset tokens is a generally an exempt supply, and the issuance of utility tokens is considered a taxable supply if no specific exemption applies. The proceeds from the sale of crypto-assets generally constitute income for the issuer, unless the asset sold is a debt instrument.

In sum, the possible tax consequences for the parties involved in cryptocurrencies transactions must be analysed on a case-by-case basis under current federal and cantonal tax laws (and existing guidelines). It is generally possible to confirm the Swiss tax treatment in a binding advance tax ruling. For ICOs and other significant transactions, arranging a tax ruling is best practice.

2.9 Other Government Initiatives
In 2018, the State Secretariat for International Financial Matters established a Blockchain Task Force to look into the benefits of the technology. Based on the work of a federal expert group, the Federal Council published a report on 14 December 2018 on the legal framework for DLT and blockchain applications in Switzerland. The report was intended, inter alia, to serve as a basis for the Federal Department of Finance and the Federal Department of Justice and Police to prepare a legislative proposal.

3. CRYPTOCURRENCIES AND OTHER DIGITAL ASSETS

3.1 Ownership
In the context of cryptocurrencies and blockchain, digital assets can be divided into two types of cryptocurrency (or token) from a Swiss civil law perspective.

- First, cryptocurrencies (such as bitcoin) that primarily represent a value within the blockchain context, the value of which is limited to applications on the blockchain. Such tokens cannot be characterised as property (rights in rem), securities or uncertificated securities, or rights. There is thus no specific requirement for the valid transfer of such tokens (or claims to such tokens) from a civil law perspective. In other words, the transfer may occur without any formal requirements by making the de facto power-of-disposal (or access) available to the transferee or any third party.
- Second, tokens that are intended to represent (tradable) rights existing outside the blockchain and fulfil the purposes of securities that can be transferred via the blockchain, for which formal requirements must be fulfilled (so-called ledger-based securities). A ledger-based security is a right that is registered in a securities ledger in accordance with an (registration) agreement between the parties. To create and transfer ledger-based securities, the securities ledger must meet the following requirements:
  - (a) it must give the creditors, but not the debtors, power of disposal over their rights by means of technical procedures;
  - (b) its integrity must be protected from unauthorised modifications by appropriate technical and organisational measures;
  - (c) the content of the rights, the functioning of the ledger and the registration agreement must be recorded in the ledger or in accompanying data linked thereto; and
  - (d) creditors may view the information and ledger entries concerning them and check the integrity of the content of the ledger concerning them, without the assistance of third parties.

Unlike the transfer of uncertificated securities, the transfer of ledger-based security does not require a written deed of assignment. For exam-

ple, a purchase agreement (legal basis) and the actual transfer of the ledger-based security via the entry into the distributed ledger are sufficient for a valid transfer of ownership. Both fungible and non-fungible tokens (NFTs) can be issued as ledger-based securities (or rights).

The DLT Bill does not explicitly answer the general question as to when the transfer of such securities (digital assets) is final; the answer will depend on the underlying technology and the (registration) agreement between the parties.

However, if the creditor of a ledger-based security becomes bankrupt, for example, after it disposed of a ledger-based security, the DLT Bill provides that such disposal will be legally binding and effective towards third parties if it became irrevocable according to the distributed ledger's rules (or any other trading system) and it has actually been entered into the ledger within 24 hours.

3.2 Categorisation
In broad terms, digital assets (such as payment tokens, utility tokens and security tokens) are classified as intangible assets that can be the object of contractual agreements. The prevalent categorisation of digital assets initially stems from FINMA and distinguishes between three types of tokens: payment tokens, utility tokens and asset tokens.

This token categorisation and the treatment of tokens by FINMA are rather straightforward from the perspective of the Swiss financial market laws. FINMA's focus is on the economic function and purpose of a token (substance over form), and follows the principle of "same risks, same rules", while taking into account the specific features of each project.

Payment Tokens
These are synonymous with cryptocurrencies, such as bitcoin, and are tokens that are intended to be used, now or in the future, as a means of payment for acquiring goods or services, or as a form of money or value transfer. Cryptocurrencies give rise to no claims on their issuer, so FINMA will not treat payment tokens as securities. However, if payment tokens were to be classified as securities through new case law or legislation, FINMA would accordingly revise its practice.

Utility Tokens
These are tokens that are intended to provide access digitally to an application or service by means of a blockchain-based infrastructure. FINMA will not treat utility tokens as securities if their sole purpose is to confer digital access rights to an application or service and if the utility token can actually be used in this way at the point of issue. In such cases, FINMA is of the view that the underlying function is to grant access rights, and the connection with capital markets – which is a typical feature of securities – is missing. However, if utility tokens have an investment purpose at the point of issue, either additionally or solely, FINMA will treat such tokens as securities in the same way as asset tokens.

Asset Tokens
These represent debt or equity claims on the issuer. Asset tokens promise, for example, a share in the future company earnings or future capital flows. In terms of their economic function, therefore, these tokens are analogous to equities, bonds or derivatives. Tokens that enable physical assets (such as commodities or real estate) to be traded on the blockchain would also fall into this category, so FINMA will treat asset tokens as securities if they represent an uncertificated security and the tokens are stand-

ardised and suitable for mass standardised trading.

3.3 Stablecoins

Stablecoins are currently not governed by any specific regulation in Switzerland. FINMA's treatment of any stablecoins under supervisory laws follows its existing approach for blockchain-based tokens.

Thus, stablecoins backed by deposits of fiat currency or by "algorithmic" stabilisation mechanisms are neither payment tokens per se nor security tokens per se. In any case, stablecoin projects often give rise to potential licensing requirements.

For example, a stablecoin backed by deposits of fiat currency with a fixed redemption right of the token holder may be subject to the Swiss banking regulation. If that stablecoin project would also qualify as a payment system, it may additionally be subject to the Financial Market Infrastructure Act, provided that the payment system reaches the threshold of "significant importance" to the Swiss economy. Should the stabilisation mechanism depend not on the issuance and redemption of tokens and the sale or purchase of a currency but, alternatively, on the price development of a basket of currencies or commodities, which is managed by the system's operator, there is the risk that the stablecoin and the issuer will be subject to the Collective Investment Schemes Act.

Finally, FINMA has found that AMLA is "almost always" applicable to stablecoins and the issuer, as the payment feature usually appears to be a pivotal element. Applying this approach to stablecoins linked to currencies, commodities, real estate or securities, for example, will prompt any issuer or sponsor of stablecoin projects to pre-assess the project from a supervisory perspective, particularly with respect to Swiss banking regulation, financial market infrastructure regulation, securities and funds regulation and anti-money laundering regulation.

3.4 Use of Digital Assets

In Switzerland, payments for goods and services made with cryptocurrencies are basically allowed and there are no specific cryptocurrency-related limits. For such payments, the general principles of Swiss civil laws apply, notably contract law. Hence, the limitations that do apply are to be found in the Swiss Code of Obligations, for example, which sets out the material and formal requirements for the valid entry into and performance of agreements such as purchase agreements, service agreements and employment agreements.

3.5 Non-fungible Tokens

No specific regulation applies to the sale of NFTs, which, unlike fungible tokens, are not interchangeable. NTFs are usually non-divisible in nature and are thus amenable to blockchain projects related, for example, to the digitisation of unique objects (such as pieces of art, luxury goods and real estate), digital identity and digital certifications.

From a Swiss financial market supervisory perspective, it can thus not be excluded that the issuance and/or transfer of such tokens will be subject to some degree of financial market regulation. In broad terms, the general principles of law and existing statutes will apply – regarding, for example, data protection, intellectual property, and creditor and investor protection.

4. EXCHANGES, MARKETS AND WALLET PROVIDERS

4.1 Types of Markets

Digital assets can be traded or exchanged peer-to-peer in the blockchain network or by using

cryptobanks, cryptobrokers, crypto-exchanges or crypto trading platforms.

The Swiss secondary market for trading digital assets currently consists of these market participants (or stakeholders). Furthermore, there is a market for exchange-traded products whose underlyings are, for example, bitcoins or ethereums.

4.2 On-Ramps and Off-Ramps

Usually, persons exchange fiat currencies for cryptocurrencies (and vice versa) or cryptocurrencies for cryptocurrencies at crypto-exchanges, cryptobanks and cryptobrokers, or cryptotrading platforms. Before such persons can use the exchange or trading services of the respective platform's operator, they must register and undergo an anti-money laundering/know your customer (AML/KYC) check. Once the onboarding procedure is completed, they may use an account or wallet provided by the platform's operator.

The exchange or "secondary trading" of cryptocurrencies at cryptobanks and cryptobrokers or crypto-exchanges occurs as follows:

- the platform's operator purchases or sells the cryptocurrencies from or to the persons as a principal; or
- it purchases or sells the cryptocurrencies as an agent of the customer.

By contrast, the exchange or "secondary trading" of cryptocurrencies on a trading platform is usually based on a multiparty relationship – ie, cryptotrading platforms automatically match the purchase or sale orders of their clients and credit or debit the respective amounts. While the accounts offered by the platform are involved at centralised cryptocurrency trading platforms, at decentralised cryptocurrency trading platforms trades are settled directly by using the customer's blockchain address. The use of centralised cryptocurrency trading platforms is currently more common in Switzerland. As crypto-exchanges, cryptobanks, cryptobrokers and centralised cryptotrading platforms qualify as financial intermediaries, they are required to apply the AML identification and monitoring rules upon the commencement of the client relationship and during the execution of money transmission transactions. As financial intermediaries, they must be directly supervised by FINMA or be affiliated with an SRO.

4.3 KYC/AML

AMLA states that financial intermediaries are persons who, on a professional basis, accept or hold onto deposit assets belonging to others or who assist in the investment or transfer of such assets.

They include persons who provide services related to payment transactions, in particular by carrying out electronic transfers on behalf of other persons, or who issue or manage means of payment such as credit cards, travellers' cheques or virtual currencies, or who accept such virtual currencies.

In principle, persons transferring digital assets such as payment tokens may qualify as financial intermediaries and, as such, they are subject to both the simplified and the enhanced due diligence duties. For example, a cryptobroker must identify the customers with which it is dealing and determine the beneficial owner of the assets.

Furthermore, if legal entities are customers of a cryptobroker, the broker must determine the controlling persons of those legal entities and be provided with certain corporate documents and powers of attorney. Under certain circumstances, the cryptobroker must also clarify the economic background and the purpose of a crypto transaction or of a business relationship

(eg, if the transaction or the business relationship appears unusual or if the transaction or business relationship appears to be very risky).

4.4 Regulation of Markets

As mentioned in **3. Cryptocurrencies and Other Digital Assets**, the existing laws apply to markets for digital assets. The implementation of digital asset projects often gives rise to potential licensing requirements under financial market supervisory laws. In this respect, FINMA is the competent regulator or supervisor to monitor compliance with Swiss financial market regulation. Additionally, if there is suspected illegal conduct with respect to other areas of regulation (such as antitrust laws, tax laws, criminal laws or unfair competition), other authorities may become involved (eg, federal or cantonal prosecutors, administrative authorities or courts).

4.5 Re-hypothecation of Assets

In Switzerland, there is no specific blockchain regulation applicable to the re-hypothecation of crypto-assets.

4.6 Wallet Providers

In Switzerland, there is no specific blockchain or cryptocurrency regulation that is applicable to wallet provision. In practice, cryptobanks, cryptobrokers, crypto-exchanges and cryptotrading platforms offer custodian services, as well as cryptocustodians. In particular, cryptocustodians (such as XAPO) are specialised companies that offer hot and/or cold storage of digital assets for their clients.

Hot or cold storage solutions for private cryptographic keys must be assessed on a case-by-case basis from a Swiss banking regulation perspective. As a matter of principle, if clients' assets are commingled or the service provider has the sole power of disposal over the clients' assets, there is an imminent risk for the service provider that the services will be regulated under the Swiss Banking Act.

5. CAPITAL MARKETS AND FUNDRAISING

5.1 Initial Coin Offerings

In Switzerland, there is no regulation specific to ICOs. As mentioned in **3. Cryptocurrencies and Other Digital Assets**, the existing laws apply to this kind of fundraising. FINMA will apply financial market laws if the issuance of tokens and/or the commercial activity qualify either (i) as payment tokens or asset (security) tokens, or (ii) as regulated business activity (such as banking activity, securities dealing activity or financial intermediation).

As a matter of principle, FINMA will apply the principles of "substance-over-form" and "same risks, same rules". For example, FINMA will first categorise the ICOs and if, for example, an ICO qualifies as a securities token offering, FINMA will analyse whether the securities offering complies with the Swiss Financial Services Act, the Swiss Collective Investment Schemes Act and/or the Swiss Financial Market Infrastructure Act (whichever is applicable). FINMA will then analyse the commercial activity and assess whether it is centralised or decentralised. For example, if the token issuer operates, on a commercial basis, a centralised trading platform through which the token holders may trade or exchange their tokens, FINMA may qualify the issuer as a securities firm or a trading facility subject to the Swiss Financial Institutions Act or the Swiss Financial Market Infrastructure Act (whichever is applicable).

5.2 Initial Exchange Offerings

In Switzerland, there is no specific blockchain or cryptocurrency regulation applicable to initial exchange offerings (IEOs). The same principles

apply as mentioned in **3. Cryptocurrencies and Other Digital Assets** and **5.1 Initial Coin Offerings**.

5.3 Investment Funds

In Switzerland, there is no specific blockchain or cryptocurrency regulation applicable to crypto-investment funds or collective investment schemes that invest in digital assets.

FINMA applies the existing Swiss Collective Investment Schemes Act and the respective ordinances to crypto-investment funds. Such funds would qualify as alternative investment funds subject to certain investment rules. Crypto Fund AG is currently the only licensed asset manager for cryptofunds in Switzerland.

5.4 Broker-Dealers and Other Financial Intermediaries

In Switzerland, there is no specific blockchain or cryptocurrency regulation applicable to broker-dealers or other financial intermediaries that deal in digital assets. As a matter of principle, FINMA applies existing financial market regulation on a case-by-case basis to assess whether a licence is required.

6. SMART CONTRACTS

6.1 Enforceability

In Switzerland, there are no laws, regulations or binding judicial decisions addressing the legal enforceability of smart contracts. Swiss legal doctrine largely agrees that a smart contract is not a contract in the sense of the Swiss Code of Obligations.

Due to the automated character of a smart contract, the application of civil law principles concerning the formation and execution of traditional contracts to smart contracts raises questions. According to the prevailing doctrine, a computer system lacks the legal personality required to enter into a contract. There might also be legal uncertainty due to the pseudonymity of the users or participants in blockchain networks, and even their legal capacity to initiate transactions that are then automatically executed by the smart contract could be questioned. The legal validity of arrangements related to smart contracts is not, however, prima facie excluded.

6.2 Developer Liability

As existing legal principles apply to blockchain technology, the legal risk of developers being held responsible for losses, as injuring party or tortfeasor based on contractual or tort law (eg, liability for programming errors, technical program effects, or any technical flaws), cannot be excluded.

Furthermore, pursuant to the DLT Bill, the obligor under a ledger-based security is liable for damage to the acquirer arising out of information that is inaccurate, misleading or in breach of statutory requirements, unless the obligor can prove that he or she acted with due diligence. Consequently, if an obligor were to use a specific blockchain technology in order to issue tokens, it might be held liable if that technology had flaws and caused losses to the token holders.

7. LENDING, CUSTODY AND SECURED TRANSACTIONS

7.1 Decentralised Finance Platforms

The operation of DeFi platforms is not prohibited in Switzerland, where there is no specific blockchain or cryptocurrency regulation applicable to DeFi platforms. As mentioned in **3. Cryptocurrencies and Other Digital Assets** and **5. Capital Markets and Fundraising**, FINMA applies the existing financial market regulation on a case-by-case basis to assess whether a

licence is required for the platform's operation. As a matter of principle, there is the risk that cryptocurrency lending activities will be subject to Swiss banking regulations.

7.2 Security

Generally, a lender can take collateral for a loan in the form of a pledge or a transfer of "ownership" of claims by entering into a separate security agreement. Claims can either be pledged or assigned for security purposes.

In terms of digital assets, the DLT Bill sets out that a collateral (eg, lien) can also be established without transferring the ledger-based security if the collateral is visible in the ledger and, at the same time, it is guaranteed that only the security taker can dispose of the ledger-based security in the event of default.

7.3 Custody

Under Swiss law, investors or token holders can deposit their digital assets with third parties and provide collaterals via custodians (as discussed in **7.2 Security**). A custodian may qualify as a financial intermediary and be subject to Swiss financial market regulation, notably Swiss anti-money laundering regulation; hence, a custodian will be required to affiliate with an SRO Should that custodian take deposits, it may also be required to obtain a licence as a fintech company or bank in Switzerland.

8. DATA PRIVACY AND PROTECTION

8.1 Data Privacy

The exercise of data subjects' rights is particularly demanding and subject to the general principles of Swiss civil law, notably the Federal Act on Data Protection, according to which data subjects have a legal right to information, rectification, revocation and deletion. The right to information entitles data subjects to request information from the data controller on whether data relating to them is being processed. The other rights of data subjects are essentially aimed at correcting false, incomplete and/or redundant data. Since public blockchains do not have a central control body and there is consequently no central person responsible for data protection, the enforcement of these rights (including the "right to be forgotten") are de facto impossible.

Hence, a blockchain should be designed in a way to comply with Swiss laws and regulation. For example, if the person concerned consents to data processing before using a blockchain or blockchain-related product, the specific processing of that individual's data within the scope of such application and to the extent of that consent is not unlawful. Furthermore, "chameleon hash functions" may enable data on a blockchain to be deleted under certain conditions, or the storage of data off-chain, while limiting the on-chain data to hash values may be a permissible privacy design under Swiss privacy laws.

8.2 Data Protection

In principle, when personal data is processed, the Federal Act on Data Protection applies. Accordingly, and firstly, personal data is all information relating to an identified or identifiable person.

A person is identified when information clearly establishes the identity of that individual. The person is identifiable if their identity can be inferred on the basis of additional information. The existence of personal data must be assessed on a case-by-case basis and in consideration of the specific circumstances.

Therefore, it cannot be excluded that data stored on blockchains, or blockchain-related products or services, can be regarded as personal data

if there is actual or legal access to additional information that enables the person concerned to be identified. Secondly, the processing of data means any operation with personal data, irrespective of the means and procedures applied, in particular the collection, storage, use, modification, disclosure, archiving or destruction of personal data. Data processing in that sense occurs when a node is added to a blockchain, and the block is duplicated and saved again. Processors of this data are all participants in the system (namely the initiator of a transaction, the receiver, and the party who validates a transaction under the consensus mechanism). Swiss law requires each of these processors to comply with the principles of transparency (recognisability of data procurement and its purpose), purpose limitation, proportionality, correctness and security of the data.

9. MINING AND STAKING

9.1 Mining
Mining activities are allowed in Switzerland.

The mining of cryptocurrencies, confirming transactions and validating blocks do not constitute financial services per se, nor are they deemed to be regulated activities subject to Swiss financial market regulation.

That said, if, for example, a mining company domiciled in Switzerland validates transactions and is rewarded with cryptocurrency (such as bitcoins), that company should not qualify as a financial service provider or financial intermediary.

However, if the mining company involves third party assets and carries out the mining activities on behalf of others, it may be deemed a financial intermediary, which could trigger licensing or registration activities subject to Swiss financial market regulation.

9.2 Staking
Staking activities are allowed in Switzerland.

Staking processes and activities, for example based on proof of stake (PoS) consensus protocols, do not constitute financial services per se, nor are they deemed to be regulated activities subject to Swiss financial market regulation. Depending on the business models, however, the use of such protocols by an intermediary to provide staking rewards to investors may have regulatory implications in Switzerland.

For example, if tokens are created on a PoS consensus protocol that have integrated "token farming functionalities" (ie, asset pools being deploying for various staking processes), an issuer and operator of such tokens could resemble the activities of an asset manager. In such a case, it cannot be excluded that the Swiss Financial Institutions Act and the Swiss Collective Investment Schemes Act may apply to the operator. As a matter of principle, FINMA applies existing financial market regulation to any crypto business model, if required.

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Pestalozzi is a multicultural Swiss business law firm focusing on high-end work for domestic and international clients since 1911. Pestalozzi lawyers are strong and empathic personalities, known for their truly independent approach to advising and representing their clients. The firm guides and supports its clients in their strategic business decisions, anticipates their future challenges and helps them solve their critical issues. Being fully integrated, Pestalozzi encounters no internal limits in shaping the most competent and efficient teams for clients' needs. With more than 100 professionals in Zurich and Geneva, the firm is at home in Switzerland's two main commercial hubs – and has developed a wealth of experience in its key industries of banking, life sciences, commodity trading and insurance. While being locally embedded, Pestalozzi has also developed sought-after expertise in dealing with multi-jurisdictional transactions and disputes.

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