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Fula Governance Association

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Token Analysis – \$FULA Token

This analysis of the \$FULA Token (“**\$FULA**”) is based on Swiss regulation:

- FINMA’s Guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs), published 16th February 2018;
- Federal Law on Anti-Money Laundering and Combating the Financing of Terrorism (Anti-Money Laundering Act (“**AMLA**”), SR 955.0, as of 18th February 2020);
- Ordinance on Anti-Money laundering and Combating the Financing of Terrorism (Anti-Money Laundering Ordinance (“**AMLO**”), SR 955.01, as of 11th November 2015);
- FINMA Circular 2011/1 Activity as a financial intermediary under the AMLA (“**FINMA Circular 2011/1**”) dated 26th October 2016;
- Supplement to the guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs), published 11th September 2019;
- Ending the Rental Webb Whitepaper (“**Whitepaper**”), undated;
- Token one pager, undated;
- Emails dated 5th September 2023.

This analysis covers the token classification of \$FULA and its implications.

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Overview

According to the information provided, the Fula network is a privacy-focused, user-owned, free-to-use and open source decentralized resource network (“**Network**”). The Network employs a new kind of proof, the Proof of Resource (“**PoR**”) mechanism. The Network uses shared resources such as computation and storage to verify transactions. Storage is provided either by a plug-n-play decentralized app (“**dApp**”) server (a hardware “**Box**” device) or via a pool of independent providers. The community of the Network consists of miners, devices and dApps developers and is driven by the protocol's \$FULA token. An end user (“**End User**”) pays for using services on the Network without owning a connected hardware device, by paying for the usage of both resources and dApps. Miners earn \$FULA by providing resources, validating transactions and integrity of the Network. DApps developers earn \$FULA for providing dApps to the Network.

The Network is based on a three-layer (L1-L3) chain system. Fula L1 is the Global Ledger of \$FULA on Ethereum. Fula L2 is multichain and includes individual chains such as Polkadot, Cosmos and Algorand, as well as rollups such as Arbitrum, Polygon, etc. Fula L3 is the pool-chain which uses Proof of Resources to verify all transactions on a given pool of computers (“**Pool**”) that share resources.

Issuer

The issuer of \$FULA is the Fula Governance Association (“**Issuer**”), a Swiss association within the meaning of Article 60 et seqq. of the Swiss Civil Code. The Issuer (while maintaining its legal structure as association) eventually evolves into a decentralized autonomous organization (“**Fula Governance DAO**”) owned and led by its members.

\$FULA

\$FULA is ERC-20 token and can be used for:

- Governance of the Network
- Paying to use storage and CPU power from a Pool

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- Paying to use a dApp;
- Users to earn \$FULA for providing CPU and storage resources;
- Users to earn rewards from transactions fees, as well as for validating the integrity of the Network;
- DApp developers to receive \$FULA for providing dApps to the Network.

Token Features of the \$FUL

Access	By holding \$FULA a user becomes a member of the Network respectively a member of the DAO (" User ").
Governance	The governance of the Network is enabled through \$FULA. Token holders are eligible to vote and make proposals. To participate in the governance of the Network, holding \$FULA is sufficient. There is no need to stake or lock \$FULA in order to participate in the governance. The voting power of a user is linked to the number of \$FULA he or she holds..
Rewards	The Network provides a utility sharing \$FULA reward in addition to the validation reward. As more users join the Network, mining rewards decrease, but the utility sharing reward remains constant and is not affected by the number of Users. All Users in an L3 Pool participate in the validation process and will be rewarded. The box owner can earn more \$FULA by allocating resources to the Pools. Each Pool has its own criteria for resource allocation to join. The total annual mining reward for the first two years is 120m \$FULA which equals a monthly reward of 10m \$FULA distributed among all Users providing storage/resources.
Payment	Users have to pay in \$FULA for storage and Central Processing Unit (CPU) power from an L3 Pool as well as for the use of dApps.

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The End User's payment for resources usage is measured and given a value (1 \$FULA), which then is distributed between those who provide the resource (e.g. 70%) and the remaining 30% is paid to the dApp developer and software dependencies. The remaining 10% of the dApp development transactions are paid to the Fula Governance DAO Network's treasury.

Miners earn \$FULA for providing CPU and storage resources, as well as for transactions and validations on the integrity of the Network. DApp developers earn \$FULA for providing dApps to the Network. When an End User uses a dApp, the smart contract executes the token transfer from the End User to the dApp developer.

Staking Users may claim their earned \$FULA (see above). These claimed \$FULA are unlocked and Users as well as End Users may stake their \$FULA in their wallets. End Users may stake \$FULA on most promising applications as well as stake for fee reduction (with lockup period which will be defined at a later stage). Staking also allows Users to earn additional \$FULA rewards.

Token

Classification

The Swiss Financial Market Supervisory Authority (**"FINMA"**) assesses tokens based on the underlying purpose of token and the economic function. FINMA categorizes tokens into three types which are i) payment tokens, ii) utility tokens and iii) asset tokens.

Payment Token Payment tokens or cryptocurrencies are tokens which are intended to be used, now or in the future, as a means of payment for acquiring goods or services or as a means of money or value transfer.¹ Where the token is intended to function as a

¹ FINMA Guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs), Published 16th February 2018, p. 3.

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means of payment and can already be transferred, FINMA requires compliance with Swiss anti-money laundering regulations. FINMA will not, however, treat such tokens as securities.

Utility Token Utility tokens are tokens, which are intended to provide digital access to an application or service by means of a blockchain-based infrastructure.² If the sole purpose of the token is to confer digital access rights to a Network, application or service and if the utility token can already be used at the point of issue, this token does not qualify as security.

Asset Token Asset tokens represent assets such as a debt or equity claim on the Issuer. For example, asset tokens can represent a share in future company earnings or capital flows. The economic function of these tokens is analogous to equities, bonds or derivatives. Tokens that represent physical assets and can be traded on the blockchain fall into this category.

Generally, FINMA regards asset tokens as securities, which means that there are securities law requirements for trading in such tokens, as well as prospectus requirements imposed by the new Financial Services Act (FinSA). A self-issuance does not generally trigger licensing requirements, but the acquisition and primary market offering of corresponding token can constitute an activity as a security issuing company.

² FINMA Guidelines for enquiries regarding the regulatory framework for initial coin offerings (ICOs), Published 16 February 2018, p. 3.

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Analysis of the \$FULA

Access/ Governance

\$FULA gives the holders access to the Network blockchain-based infrastructure, meaning Users can only access the Network with \$FULA and use the Network's dApps and resource provided by L3 Pools.

Furthermore, \$FULA gives holders the right to vote on governance related matters (e.g. rewards and revenues). The voting power equals the number of \$FULA held by a User.

As \$FULA gives Users digital access to the Network and its services, it will be qualified as a utility token according to FINMA's token classification.

Payment

FINMA could classify \$FULA as payment token or more precisely as a hybrid utility-payment token. The issuer of such payment token could therefore be considered as a financial intermediary and would need to become an affiliate of a self-regulatory organization ("**SRO**") and comply with the Swiss AML regulations. In other words, the Issuer would need to identify \$FULA purchasers either by means of an in-person identification process or by correspondence, or by means of the online or the video identification process according to FINMA Circular 2016/7.

The qualification could be different, however, if it is ensured that the use of \$FULA is confined to the Network and that \$FULA can only be used as a means of payment between the Issuer and the members i.e. that \$FULA can only be used within the Fula ecosystem. Under these circumstances it can be argued that while the \$FULA qualifies as a means of payment its issuance is not subject to the Swiss anti-money laundering regulations. More specifically and according to FINMA Circular 2011/1 para. 64* the issuance of a means of payment is only subject to the Swiss

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anti-money-laundering regulation if the Issuer is not identical with the users of the means of payment, i.e. if (at least) a three-party relationship exists. If the Issuer (or its affiliated partners) of the means of payment (i.e. the payment token) is also the seller of a good for the payment of which the means of payment is used, there is a normal two-party relationship and the Issuer is not regarded as a financial intermediary (and hence not subjected to the anti-money-laundering regulation). As long as this two-party relationship between the Issuer and the token holders is maintained the issuance of the payment token will most likely not be subject to Swiss anti-money laundering regulations and the Issuer will accordingly not be considered as a financial intermediary.

The Issuer of \$FULA is the Fula Governance Association. \$FULA is used to pay for the services offered on the Network, e.g. usage of resources and dApps provided by other Network community members (miners and dApp developers). The “sellers or providers” of the services are part of the Network community. The seller and the Issuer are both using the Network and are part of the Fula community. Therefore, the two-party relationship is still ensured. As \$FULA is only used within the Fula ecosystem and not intended to be used as a widely adopted payment token, the Issuer will not be qualified as a financial intermediary.

Furthermore, assisting in the transfer of crypto currencies (payment token) to another person (third party) or exercising power of disposal over crypto currencies, will be considered a payment transaction service within the meaning of art. 2 para. 3 letter b AMLA provided that there is a permanent business relationship with the customer or user. This means that if the Issuer helps transferring \$FULA token from one User to another – for instance when an End Users pays \$FULA to the dApp developer and the Issuer is involved in the transaction – the Issuer would be

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considered a financial intermediary under the AMLA. However, if the transfer of \$FULA, is executed completely automatically via smart contract or if the User him-/herself can execute the transfer and the Issuer has no power of disposal including no power to block the execution, the Issuer is most likely not be considered a financial intermediary.

According to the information provided, the token flow i.e. the transfer of \$FULA will be executed automatically by smart contracts without the possibility of any interference of the Issuer. Since \$FULA token qualifies as a hybrid utility- payment token, it is important to note that pooling (jointly storing tokens) third party's \$FULA and thus, providing the storage provider access to the corresponding private keys, thereby granting control (power of disposal), will be regarded as custody of third-party deposits, potentially necessitating a Fintech or even a banking license. Based on the documents and information, staking services and activities are fully decentralized and automatically executed without the involvement of the Issuer. Therefore, staked \$FULA tokens remain under full control of the wallet owners (as the Issuer has no access to the private keys) and a Fintech or even banking license is not required. However, to fully exclude the requirement of having a banking or Fintech license we would need to analyse the treasury activities, further information on who holds the private keys as well as the power of disposal (control) of the locked funds.

The Network treasury may be qualified as a collective investment scheme under the respective Act ("**CISA**"). According to art 7 para. 1 CISA collective investment schemes are assets raised from investors for the purpose of collective investment, and which are managed for the account of such investors. The investment requirements of the investors are met on an equal basis and managed by a third party. Once there is clarity on who has access to the private keys and how the

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treasury's token distribution is executed (automatically or not), an assessment of whether it qualifies as a collective investment scheme is necessary. Where the token flow is executed by a smart contract, third party interference is factually not possible and the Network treasury would not qualify as collective investment scheme.

Asset token

\$FULA holders respectively DAO members will be able to influence the distribution of rewards to the Users (miners, stakers and dApp developers). As per FINMA's practice, the right to influence the revenue distribution is similar to the shareholders' right to vote on the distribution of their dividends. Hence, FINMA maintains the perspective that these tokens, akin to shares, should be classified as securities. However, this approach may not be appropriate for decentralized networks like the Fula Network, where rewards are distributed by the community (rather than the issuer) as remuneration for their members' service contributions to the Network. Nevertheless, FINMA adheres to this practice.

Since the \$FULA token serves as both a utility and payment token, when voting on \$FULA rewards, similar to a dividend, monetary value is distributed to the Users.

Therefore, there is a substantial risk that FINMA might classify \$FULA as a security token. To mitigate this risk, it is necessary to relinquish the capability for Users to vote on their own revenue rights.

Furthermore, it must be ensured that \$FULA can be used at the point of issuance already. The utilities must be established; otherwise, there is a strong likelihood that FINMA will not classify the \$Fula token as a security token.

Conclusion

- \$FULA holders have access and governance rights on the Network. Hence, \$FULA is a utility token according to the FINMA token classification.

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- There is a probability that FINMA would qualify \$FULA as a hybrid utility-payment token. The issuer of a hybrid utility-payment token is generally considered a financial intermediary and thus, Swiss anti-money-laundering regulation will be applicable to the token issuer. However, it could be argued, that the \$FULA token qualifies as a means of payment which is not subject to Swiss anti-money-laundering regulation since the intention is that \$FULA will only be used and accepted within its own Network. In this case, the Issuer and Users of the means of payment are both part of the Network itself. Under these circumstances the Issuer would not be qualified as financial intermediary.
- However, if \$FULA is also to be accepted (or intended to be accepted) outside of the Network (i.e. if there was to be a three – or more – party relationship) already at the point of issuance FINMA would qualify the \$FULA token as a payment token which is subject to Swiss anti-money-laundering regulation and the Issuer would accordingly qualify as financial intermediary. As a financial intermediary the Issuer would need to become an affiliate of an SRO and comply with the Swiss AML regulations or outsource the financial intermediation to a third-party provider with the respective SRO affiliation.
- Even if the Issuer will not be qualified as a financial intermediary it is highly recommended to identify purchasers of \$FULA tokens when tokens in the amount of CHF 15,000 or more are being purchased.
- Apart from the issuance of a means of payment, the distribution of \$FULA by the Network could still be considered as a financial intermediary service (Article 4 para. 1 let. c AMLO in conjunction with Article 2 para. 3 let. c AMLA). In case that the distribution of \$FULA is actively managed by the Association (by orchestrating payments from one User to another or out of the treasury, distributing staking rewards etc.), the Association would then qualify as a financial intermediary for providing financial services. For the Fula Network the whole token flow (revenue

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distribution for staking and providing storage as well payment for using dApps) is handled completely automatically (e.g. by a smart contract), the Association has no power to intervene in such transactions. There is no room for proactive management of the tokens. No financial services are offered, and the Association does therefore not qualify as a financial intermediary. In any way, KYC-checks as mentioned before (purchase worth CHF 15,000) should still be executed.

- To avoid the need for a banking license or Fintech license for the Network's treasury, more information on the storage conditions and access to the respective private keys is required.
- Since \$FULA token holders are able to vote on their own revenue distribution, i.e. staking rewards and earnings, \$FULA is most likely to be considered a security token under the current FINMA practice. However, by relinquishing the voting right on the revenue distribution and provided that \$FULA does not function solely as an investment (could be the case if the utilities are not established at the time of issuance), \$FULA will most likely not be considered a security token under Swiss regulation.
- If the \$FULA revenue voting power remains unchanged, we recommend to submit a ruling request to FINMA and contest their existing approach.

Kind regards,

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