

LEGAL MEMORANDUM
REDL token analysis

General Provisions

Corporate structure.

The issue and sales of the REDL tokens are conducted by the FINTECH FOUNDATION OÜ, 14365981, registered in Estonia, and created in order to develop the Platform and provide services, operational control, and maintenance of the Platform.

The RED LANTERNS Platform is a digital platform, based on the blockchain technology, of processing and access to data, digital services, meant for getting/giving advisory and other services all over the world using Ethereum based smart contracts. The Platform is available in the mobile app implemented for Android and IOS available for download in GOOGLE PLAY MARKET and APP STORE.

The REDL is a digital utility token, implemented based on the Ethereum public blockchain as the ERC20 Ethereum token, that can be used to get access to the services and functionality of the platform, and services provided on the Platform.

Documents provided by the Company for information:

White Paper, the REDL Token Sales Agreement , The Disclaimer (included in the text of the REDL Token Sales Agreement).

Analysis of the legislation of the Republic of Estonia, that regulates primary placement (issue) and sales of tokens.

The Estonian Financial Supervision Authority, that regulates financial services market and functions as the Financial Supervision Authority (EFSA), established in the legal framework of initial coin offering in Estonia that the issued tokens depending on their structure and actual function might be considered as securities according to the definition set forth in the current Securities Market Act (SMA) as well as in the Law of Obligations Act (LOA).

Particularly, token issue giving the investors certain shares in the project or whose value is tied to the future profits or success of a business are likely to be considered securities, and will be governed by the rules as prescribed in § 12 of the

SMA. Secondary trading of such tokens may be considered as providing investment services as stipulated in § 43 of the SMA.

The EFSA notes that ICOs may also be governed by the Credit Institutions Act (CIA). This might be in the case where the main activity of the business is to provide loans on its own name and account and such activity is being financed through the repayable funds received from the public in the form of an ICO.

Regarding trading cryptocurrencies, it is important to mark that according to the judgement of the Estonian Supreme Court [RKHKo 3-3-1-75-15](#) (available in Estonian), trading Bitcoins as business activity corresponds to the provision of services of alternative means of payment.

With the entry into force of the Money Laundering and Terrorist Financing Prevention Act (MLTFPA) § 6(4), the respective persons should apply for authorisation pursuant to MLTFPA §-s 52(4) and 521. Through this legislation, companies that deal with virtual currencies, including cryptocurrencies can apply for 2 different licenses:

- Virtual currency service provider.
- Virtual currency wallet provider.

On the November 13, 2017, The European Securities and Markets Authority (ESMA) has issued an official Statement for investors on Initial Coin Offerings (ICOs) on risks of ICOs, and alerts firms involved in Initial Coin Offerings (ICOs) to the need to meet relevant regulatory requirements.

Consequently, under the legislation of EU and Estonia, the purpose of this memorandum is to study the following:

- legality of the REDL tokens issue and sales by FINTECH FOUNDATION OÜ in the jurisdiction of the Republic of Estonia, and compliance with the legal norms in the process of the REDL tokens issue and sales;
- definition of the legal nature of the cryptographic REDL token based on the analysis of its functionality and real purpose;
- the REDL token analysis as to the possibility of being recognized as a security, electronic money or alternative currency, electronic payment method;
- necessity of implementation of legislation related to the money laundering and terrorist financing prevention in the process of the token sales and further Platform performance, in connection with the risk-oriented approach to regulation of activities related to cryptocurrencies adopted by Estonia in November, 2017.

Based on the analysis of the questions above, the author of the Memorandum will provide several recommendations regarding the token issue and sales procedure, and minimization of possible risks on the part of the financial regulator.

Analysis of the functionality and real purpose of the REDL tokens in legal terms.

For the moment, there is no unified and coherent approach to legal definition and cryptocurrencies regulation, as well as the definition of a cryptographic token in terms of its issue and sales, due to which the legislation is applied selectively to similar products and services based on the functional purpose and nature of the risks.

Analysis of the legislation shows that a token can be characterized as a cryptographically protected confirmation of its owner's rights for receiving the promised values or possibility to function by its means in a predetermined way. Issue and functioning of the tokens are fulfilled by means of smart-contracts, which in their nature are a programming code with a pre-established order of interaction between the participants of a certain ecosystem.

As specified in the White Paper and the Token Sales Agreement, the REDL Token is a digital token, implemented based on the Ethereum public blockchain as the ERC20 Ethereum token, that can be used to get access to the services and functionality of the Platform and services provided on the Platform by means of a smart-contract.

The analysis of the documents provided by FINTECH FOUNDATION OÜ shows that the REDL Tokens do not present any guarantees or entitle their holder to a share of the company, voting right, the power to make decisions that can influence the functioning of the ecosystem.

The documents prescribe that the Token provides its holder (the Client) with the right to receive services provided by other participants of the ecosystem (the Experts) on the Platform. In addition, the specifics and characteristics of the service provision, their cost are established independently by the participants by means of a smart-contract, which ensures transparency and integrity of the service provision.

In this way, the Platform itself is an ecosystem, which provides services through smart-contracts, and whose participants may be loosely grouped into two categories: the client and the expert. The REDL Token is needed for the smart-contract to function in order to provide the exchange of information between the ecosystem participants and to confirm actions under the smart-contract.

Therefore, the REDL Token does not present any form of ordinary shares in the company, or any guaranteed form of dividend or other revenue right, or ownership rights for the products of the company, or receiving profit from the company's business activity. The REDL Token is offered for purchase solely for the use within the Platform to be exchanged for the services provided by the ecosystem participants.

The company receives certain interest from the amounts of each transaction fulfilled through the smart-contracts.

Consequently, the functional meaning of the REDL Token is in the possibility to use a smart-contract on the RED Platform in order to receive services under the contract terms and conditions.

At the same time, the Company enables the token-service exchange mechanism (token transfer from the client to the expert) and retains a commission for such exchange-transfer of the Token. The Company provides the basic conditions of the service provision, including those regulated by the smart-contract. The conditions of the Token exchange for the service are established by the participants independently and not by the Company, which indicates certain features of the REDL Token and its meaning, features characteristic of virtual currencies.

In legal terms, the Token may be considered as a utility token. However, as the Company does not provide the services to the Token Holders directly, the REDL Token exchange for the services is not directly affected by the actions of the Company, and other ecosystem participants are involved in the service provision process, the REDL Token may be considered to be a payment method and as the domestic currency in the REDL ecosystem.

The following pages contain a more detailed analysis of the legislation concerning the aforesaid.

The REDL Token legal nature analysis:

➤ *The REDL Token as a security*

According to § 917 (1)1) of the Estonian Law of Obligations Act, a security is any instrument to which a patrimonial right is attached in a manner which precludes the exercise of the right without the instrument.

As the REDL is not an ownership right and does not imply such right, the Token is not a security in the meaning of the applicable law, according to § 917 (1)1) of the Law of Obligations Act.

The issues related to securities are also regulated by the Estonian

Securities Market Act. Because the jurisdiction is a part of the European Union, the applicable rules for finance are based on The Markets in Financial Instruments Directive (MiFID).

The Law defines a security as a proprietary right or obligation or contract given over based on at least unilateral expression of will, which may constitute:

- 1) a share or any similar tradable right;
- 2) bonds, exchange security or other issued and tradable debt obligation which is not a money market instrument;
- 3) the subscription right or any other tradable right giving the right to acquire the securities mentioned in clauses 1 or 2 of this section;
- 4) a share of an investment fund;
- 5) a money market instrument;

In the opinion of the author, the REDL Token is neither a proprietary right, nor an obligation, but only provides the right to access the Platform and certain services. The REDL Tokens do not provide or guarantee their Holders any passive income. Therefore, the author does not think that the REDL Token should be qualified as a security, according to the Estonian law.

According to the Securities Act of the USA, as well as to the generally acknowledged Howey Test, the cryptographic tokens may be recognized as a security if three conditions have been met simultaneously:

- the token is offered in exchange for money or property (or cryptocurrencies, as the SEC concluded in their decision regarding “The Dao”);
- the investments must be made into the company (joint cooperation);
- the token must promise income to the investor to be received exclusively through the efforts of other people.

The White Paper and the Token sales rules analysis shows that the general model is not built on the Token speculative price increases, the possibility to receive income is not guaranteed to the Token Holders, the legal documents of the project do not guarantee any form of either regular or one-time dividend, as well as a token buy-back or token exchange.

The aforesaid allowed the Project to perform very well in taking the Howey test (the results shall be attached), which proves the unlikelihood of recognition of the Tokens as securities, or claims on the part of the national financial market regulators of the USA, Canada, China, Great Britain, Singapore, Hong Kong, South Korea, Malaysia, if selling the Tokens to their residents.

In addition, the documents include restrictions on the sale of the Tokens to the citizens of the USA, China, and Singapore.

➤ *The REDL Token as virtual money/ virtual currency*

The issues related to payment services and e-money issue are regulated in the Estonian legislation by the Payment Institutions and E-money Institutions Act.

The legal definition of e-money for the European Union countries can be found in the Directive 2000/46/EC of the European Parliament and the Council of the European Union on the taking up, pursuit and prudential supervision of the business of electronic money institutions of 18 September 2000. According to article 1 of the Directive: e-money is monetary value which expresses a monetary claim against the issuer and which:

is stored on an electronic medium;

is issued at par value of the amount of the monetary payment received;

is accepted as a payment instrument by at least one person who is not the issuer of the same e-money.

In this way, e-money is a monetary requirement (or obligation of the issuer to redeem the e-money bearer with real money) and is used to acquire goods or services from sellers.

The legal documents analysis shows that the REDL Token is used exclusively in the interaction between the ecosystem participants, is not used to buy goods or services from business enterprises, is not used to buy goods or services beyond the Platform, and the Token issuer does not undertake an obligation to redeem the Tokens.

Moreover, the “repayment” is obligatory for the circulation and functioning of e-money, since at the time the Client receives the fiat money, the e-money - a record on an electronic medium - is redeemed, that is withdrawn from circulation.

In the opinion of the author, in terms of the Estonian legislation by the Payment Institutions and E-money Institutions Act and EU legislation, the REDL Tokens can not be e-money due to the lack of all the essential characteristics.

The Company does not present an exchange of cryptocurrencies for fiat currencies, or provide services to initiate such transactions.

At the same time, although there is no official regulation of reciprocal payments in ecosystems at the moment and the EU legislation does not contain the definition of virtual currency described below, it should be noted that this terminology may be used in future as it is based on the FATF recommendations.

Virtual currency is distinguished from fiat currency (a.k.a. “real currency,” “real money,” or “national currency”), which is the coin and paper money of a country that is designated as its legal tender; circulates; and is customarily used and accepted as a medium of exchange in the issuing country. It is distinct from e-money, which is a digital representation of fiat currency used to electronically transfer value denominated in fiat currency.

E-money is a digital transfer mechanism for fiat currency—i.e., it electronically transfers value that has legal tender status.

This confirms that the Token can not be regarded as e-money. However, according to FATF recommendations, the Token shall be a decentralised convertible virtual currency, which functions as a payment mechanism.

According to this document, virtual currency is a digital representation of value that can be digitally traded and functions as (1) a medium of exchange; and/or (2) a unit of account; and/or (3) a store of value, but does not have legal tender status (i.e., when tendered to a creditor, is a valid and legal offer of payment) in any jurisdiction.

Virtual currency is not issued nor guaranteed by any jurisdiction, and fulfils the above functions only by agreement within the community of users of the virtual currency.

In this way, the FATF recommendations analysis showed that the Platform has features of a payment network in a single virtual currency, in which only one definite kind of decentralized virtual currency (single-currency) is used, and the Company itself has features of a Wallet Provider with possibility of deposits and withdrawals in the virtual currency.

The aforesaid proves the high probability of the fact that the requirements which are commonly applied to financial and credit institutions might be applied to the Company's activity, under the condition that the Platform will provide arrangements as to the Token buy/sell between the ecosystem participants, thus making it possible to store and deposit the virtual currency, as well as ensuring transfer of fiat money on transactions with this currency.

➤ *The REDL Token as a payment method*

For the purposes of the afore specified Act, “payment services” mean the following services provided by a person for the purposes of economic or professional activities:

- 1) services which enable to make cash payments to payment accounts;

- 2) services which enable to withdraw cash from payment accounts;
- 3) execution of payment transactions, including transfer of funds to a payment account opened with a payment service provider;
- 4) execution of payment transactions if the funds have been granted as a loan to the client of the payment institution;
- 5) issue and acquisition of payment means, means of payment or payment instruments;
- 6) money remittance;
- 7) execution of payment transactions if the instruction of the payer for making a payment is given by means of a telecommunications, digital or information technology device and the payment transaction is executed through a telecommunications network, information technology system or other similar network operator acting only as an intermediary between the client of the payment institution and the supplier of goods or services.

Services and transactions are not considered a payment service, and the provisions of the present Act are not applied, particularly, to the payment transactions between the payer and the receiver made by an economic agent, who on the payer's or receiver's behalf may negotiate sale or purchase of commodities or services or make sale/ purchase transactions; to the services based on instruments that might be used for purchasing commodities or services only within the issuer's territory or from the issuer of the above mentioned payment under the contract for certain services by a limited number of persons.

The author concludes that the Token does not have all the necessary features of a payment method and the activity on sale and exchange of the Tokens is not a payment service due to the limitations of the Act application.

➤ *The REDL Token in terms of financial institution*

As mentioned above, in connection with law enforcement of the Money Laundering and Terrorist Financing Prevention Act (MLTFPA), firms working with virtual currencies, including cryptocurrencies (service of alternative means of payment), must apply for an activity license to act as a virtual currency service provider or virtual currency wallet provider.

This, inter alia, obliges the Company in the future to develop and implement the internal control rules for prevention of legitimizing (laundering) of income acquired by illegal means or terrorist financing.

In this way, the Company will need to develop ways of identification and verification of the experts without personal contact, which includes: verification of

the identification data received from the client, such as the national identity card or passport number including information from foreign databases or other reliable sources; it is also possible to reveal the Internet Protocol address of the client; the Internet search for information confirming that the client's activity corresponds to the nature of their transactions, under the condition that the information is collected in accordance with the national legislation of privacy principles.

This conclusion is related to the future period of the Company's activity, because the legitimizing of illegally obtained income may be fulfilled as a result of service provision through the Platform, that is only by the specific ecosystem participant - the expert.

In case of sales of the Tokens purchased during their sales held by the Company on foreign platforms with the purposes mentioned above, the obligation to meet FATF requirements rests with the cryptocurrency exchange operator acting at a certain Exchange.

The token issue and sales analysis for compliance with the Estonian law, in terms of fundraising (crowdfunding)

It must be determined that the Estonian law does not have a corresponding act to regulate this sphere. As the financial regulator informs, one should be guided by the general rules of the law and generally accepted rules aimed at providing adequate protection and legal certainty for the investors.

In addition, crowdfunding does not require licensing, there are no uniform requirements to the firms engaged in fundraising to guarantee the protection of investors' rights, information disclosure, etc.

In the opinion of the author, issue and sales of the coins may amount to a specific kind of crowdfunding, therefore the author thinks that the Company provided sufficient information for the investor about the project, corporate structure, project team, published a warning statement of possible risks associated with the purchase of the tokens and of absence of guarantees related to the Token ownership, which is set out in the White Paper, the Token Sales Agreement, the Disclaimer.

In the opinion of the author, issue and sales of the Tokens are held in accordance with the legislation of the Republic of Estonia and the EU, without violating the law regulations.

At the same time, in the author's opinion, after the issue and sales of the Tokens, by the time the Company acts as the wallet administrator, it is possible that the need will arise for the FINTECH FOUNDATION to receive the corresponding licence necessary for virtual currencies transactions: virtual currency service provider or virtual currency wallet provider.

The structure of the process of the REDL Token issue and sales does not show features characteristic for procedures which are under supervision of the financial regulator of Estonia and which may cause negative consequences for either the investor or the Company.