Public offerings of tokens in the metaverse

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The Metaverse has the potential to revolutionize the way funds are raised from the public, by becoming an environment where public offerings of tokens are made to potential investors, represented in the Metaverse by their avatars.

Before dealing with other issues, we must first briefly explain what these much-commented tokens are, and the legal framework applicable to public offerings of tokens outside the Metaverse (i.e. in the real world).

Tokens are nothing more than digital representations of assets created in a blockchain or in other distributed ledger technologies. They are commonly divided into four categories: (i) payment tokens, which are used to transfer capital; (ii) utility tokens, which offer access to platforms, products, services and other utilities; (iii) non-fungible tokens or NFTs, which represent a unique, non-fungible asset; and (iv) security tokens, which represent an undivided interest in a company, project or enterprise.

Currently, the main tokens linked to the Metaverse are the Axie Infinity, Decentraland, and The Sandbox tokens. Each type is linked to a specific Metaverse and is essentially a utility token. There is also a profusion of non-fungible tokens, such as virtual real estate, artworks, sports cards and so on.

Public offerings of virtual assets (including tokens) have received special attention from Brazil's securities regulator, the CVM (*Comissão de Valores Mobiliários*), in recent years, particularly with the growing number of transactions to raise funds from the public through ICOs (Initial Coin Offerings) in other jurisdictions, in which investors receive tokens.

ICOs are made exclusively by digital means, which facilitates raising funds from investors in various locations in comparison to traditional offerings.

On various occasions, the CVM has made known its view that ICOs of tokens that, given their characteristics (and particularly their economic characteristics), fall within the definition of a security under article 2 of Law 6.385/1976, will be subject to Brazilian legislation and regulations governing public offerings, notably CVM Instructions 400 and 476 and CVM Guidance Opinions 32 and 33, if the tokens are offered in the Brazilian market using the means of communication identified in the governing legislation. As a rule, unless the offering falls within one of the exceptions provided for by law, the offering, the offeror and the offering coordinators must all be registered with the CVM or the Brazilian Central Bank, according to their respective jurisdictions.

Currently, however, digital exchanges (which offer trading, post-trading and custody services for digital assets) are not regulated by either the CVM or the Central Bank, and consequently, there are no token exchanges authorized to operate in Brazil. This presents a significant challenge, since the legislation and regulations applicable to Brazil's regulated securities markets, and the infrastructure for settlement and custody of securities, were not designed to accommodate ICOs but traditional physical or book-entry securities.

Given this context, we believe that the current legal framework can be transported to the Metaverse, even though that environment is strictly virtual, whenever public offerings of tokens are intended to access the Brazilian market. The biggest challenge may be in determining when an offering is directed to the Brazilian market, given that offerings are made in a virtual environment between parties manifesting as digital representations.

When an offering of tokens having the characteristics of securities is found to be made to the Brazilian market, the CVM may look at the token offering the same way it looks at ICOs, which would attract the application of the legislation and regulations governing traditional securities offerings.

Nonetheless, with the various challenges and new issues surrounding public offerings of tokens, we think that the best option is to develop a specific framework of legislation and regulations for public offerings in the Metaverse, rather than simply applying the system created for traditional securities, which does not reflect the new reality of a fully virtual environment.

>>> This article is part of the e-book "Metalaw: Reflections on Law in the Metaverse".
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