

◀ **TOKENIZED SECURITIES** ▶

REAL ESTATE ASSET TOKENIZATION



INTRODUCTION

Real estate is the largest asset class in the world. Globally, in the professionally managed industry, the size of the total real estate market reached \$8.9 trillion in 2018, up from \$8.5 trillion in 2017. That being said, the industry still suffers from significant barriers to entry. The involvement of many inefficient processes leads to expensive lending for issuers. For investors, the lack of liquidity is a stumbling block. Fundamentally, capital formation is currently difficult to achieve for issuers using traditional methods. Through tokenization, issuers can bring efficiency to many cumbersome processes, investors can access a far wider range of opportunities and liquidity can be brought to an industry that has been starved of it.



GLOSSARY

Blockchain:

A blockchain is a series of digital and immutable information stored on a public database. These blocks of data store information about transactions like the date, time, amount and so on. It also includes information about who is participating in the transactions using a unique digital signature. Each block of data is unique and are identified so by code called a 'hash'.

Smart Contract:

A key element of blockchains are smart contracts, a programmable contract with the terms of the agreement between buyer and seller being directly written into lines of code. The code and the agreements contained therein exists across a distributed, decentralized blockchain network. The code controls the execution, and transactions are trackable and irreversible.

Tokenization:

Tokenization is the process of converting an asset into a digital form that lives on a blockchain infrastructure.

Security Token:

A security token is a representation of a security on blockchain. A security token can represent all the usual financial securities like equity, debt, funds and so on.



CHALLENGES

AN INDUSTRY FRAUGHT WITH INEFFICIENCY

✗ Localized and Stagnant Assets

Private markets are notorious for being hard to access, opaque and niche for traditional investors. The markets are very local and the assets do not reach global investors in an efficient manner. For the issuer, this infrastructure makes it more difficult to raise capital since there are fewer investors. For investors opportunities to assess are limited because offerings are usually based on proximity and personal networks.

✗ Low Liquidity and Complex Portfolio Management

Real estate suffers from low liquidity because pricing and information is often unavailable and outdated. Buying and selling these investments is very difficult as the assets are priced on an ad-hoc basis. For an investor to liquidate their stake they usually involve a broker dealer who can take up to 10% in commission. Even if the investor is not in a long lock up period, unattractive fees prevent them from regularly buying and selling their investment.

✗ Siloed Data and IT Systems Handled by Service Providers

Today's global real estate market revolves around many fragmented systems and siloed networks with almost no interoperability between them. Processes such as the onboarding of investors are slow and paper-based documentation is still required. These methods are often duplicated across service providers making the onboarding process slow, inefficient and expensive.

OPPORTUNITIES

USING THE BLOCKCHAIN TO DRIVE EFFICIENCY IN REAL ESTATE

✓ Global Distribution

Replacing the current infrastructure with blockchain technology will accelerate the real estate industry into the digital era by bringing forth a global network that allows issuers to target investors globally with little added cost. Tokenized securities live on a secure digital platform and can be accessed quickly by eligible investors given they have a laptop and an internet connection.

✓ Improved Liquidity

Processes are greatly improved through tokenization as investors can quickly view their portfolio via a digital interface, use an online marketplace to find a buyer and liquidate their stake in a more efficient way. The cost for investors to buy and sell is dramatically reduced which will in turn encourage more trading in secondary markets. The interoperable infrastructure of the public blockchain and the ability to view relevant data will add more flexibility and transferability between investors.

✓ Connected Marketplace

Using the public-blockchain, market participants such as regulators, investors, transfer agents and administrators can all access relevant information on a real-time basis, allowing them to make more informed and timely decisions. For investors this enables them to fractionalize and diversify their portfolio on a wider scale because of the increased amount of opportunities at their disposal. Asset owners can automate many tedious functions such as cap table management and corporate actions.

CASE STUDY

In this hypothetical case study we will take you through all the steps required of a developer to raise funding through the issuance of a compliant tokenized real estate debt offering.

The issuer, Estate Digital, decided to choose funding through debt financing rather than equity funding. They chose this method because the company had strong financials and they anticipated they could raise the capital at a lower cost than through equity.

1 PRE-OFFERING

● Advisory Structuring

Estate Digital defined its projects in cooperation with legal, financial advisors and Tokeny Solutions. The project was to issue a total of 120 Million Euros through debt financing from institutional investors across the European Union.

Estate Digital engaged in initial discussions with their legal partner to determine the terms of the offering. They were pleased to hear that in Luxembourg the regulator passed a bill that stated it is legal to register and transfer securities using distributed ledger technology. They simply needed to follow the same rules and regulations that govern traditional securities and apply it to the new technology. Based on this the issuer chose to issue securities from Luxembourg and the tokens represented the debt. In return for lending the money, the investors became the creditors and received a promise that the principal and interest would be paid on a quarterly basis.

● Documentation

Estate Digital created all the documentation that outlined the terms of the offering. This included an offering memorandum, a document that gave all the details investors needed to know about the offering. The documentation they created included:

- ✓ **Company Overview:**
Information on the business including company profile, risks and financial information.
- ✓ **Offering Information:**
Details on minimum investment, price, rights, obligations, transfer rights, currencies, closing date and use of proceeds.
- ✓ **Disclaimers:**
Warning for investors, regulatory obligations and other disclaimers as defined with the legal party.

2 ISSUANCE

Estate Digital utilised Tokeny Solutions' ONBOARD solution to enable the qualification and digital subscription of investors and the appropriate KYC/AML duties they were obligated to perform. Once these checks were passed by investors the funds were transferred to the third party custodian. Finally, ONCHAINIDs were created and allocated to the investors, along with the security tokens.

PRODUCT SPOTLIGHT

ONBOARD

Cloud-based white-label platform enabling the digital subscription of investors. It allows issuers to streamline KYC/AML requirements, comply with regulations, distribute an offering to a global investor base and automate many cumbersome processes.

ONCHAINID

The universal identity system that allows agents, depositories, infrastructure actors and service providers to easily and securely share data with one another. The platform empowers data owners to give and revoke access to their information as they please.

T-REX (Token for Regulated EXchanges)

The globally compliant security token protocol. It is a suite of blockchain-based solutions to issue and manage compliant security tokens on a distributed infrastructure.

● Investor Qualification

As Estate Digital issued a security, they needed to make sure their investors were eligible to the offering. For this they took the terms defined by the legal party, i.e. investors limited to institutional investors in the European Union, and worked with Tokeny Solutions to ensure these obligations were reflected in the T-REX smart contracts. Investors signed up to the offering and provided all relevant documentation to prove their identity. Everytime an investor attempted to join the offering, the T-REX was engaged and the protocol validated the investor in accordance with the trusted AML & KYC parties and the legal obligations encoded in the smart contract.

● Subscription and Payment

Once the eligible investors were qualified they were able to digitally sign the subscription form and pay for their security tokens. Estate Digital chose to use a third party custodian to hold the funds collected until the round had completed. The process of collecting the funds from the investors and transferring to the custodian was handled by Tokeny Solutions.



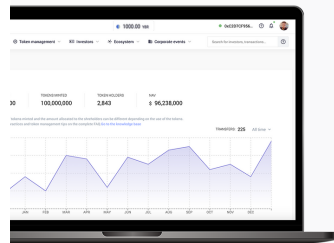
Allocation

After the funds were received the T-REX allocated security tokens to eligible investors. This allowed investors to manage their Net Asset Value from a portal to continually assess their position. The investors also received their ONCHAINIDs concurrently with their tokens.

3 POST-OFFERING

Issuers

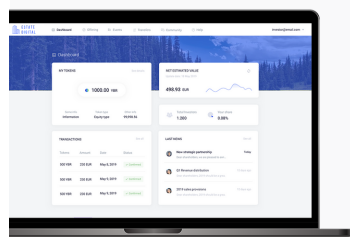
The full lifecycle of the debt instrument needed to be controlled compliantly, including the secondary trading of the security tokens. They were assured by the legal party and by Tokeny Solutions that if a trade for



their token was attempted on secondary markets the T-REX validation process would be enforced in every instance. Corporate actions such as automated reporting, quarterly dividend payouts and communications with their investors were managed via the smart contracts and the issuer portal.

Investors

Investors were able to log into a secure platform to see their positions, transfers, manage their identities and engage with corporate actions. Liquidity was improved as their investments could be liquidated easily



without subscribers paying high broker dealer fees, a process that can in some cases reach 10% using traditional methods. Baked in fees that come from inefficient processes were removed and the investors benefited from more competitive investment prices.

GOALS ACHIEVED

In less than two weeks the end to end platform was setup for Estate Digital and investors started to subscribe. Compliance was applied for every investor across the European Union and the overall goals were achieved:

- ✓ Fast and streamlined setup of the offering
- ✓ Compliant and scalable onboarding
- ✓ Successful, fast and reduced cost of fundraising
- ✓ Transferable security tokens on the global blockchain marketplace
- ✓ Direct ownership and direct link between the issuer and their investors

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