

**September 11, 2017**

## **Canadian Securities Regulators Take a Look at Cryptocurrencies**

*By Conor Cronin*

Are bitcoins a security? They might be, according to the Canadian Securities Administrators (CSA). On August 24, 2017 the CSA released *CSA Staff Notice 46-307 Cryptocurrency Offerings*. The Notice sets out concerns the CSA has related to initial coin offerings (ICO) and initial token offerings (ITO), cryptocurrency investment funds and cryptocurrency exchanges.

The CSA is an umbrella organization made up of each province's and territories' securities regulator. They coordinate on certain policies (in the absence of a national securities regulator) that affect Canada's capital markets.

This article will look at the CSA's conclusions regarding capital raising efforts made through ICOs and ITOs.

Companies considering raising capital through distributions of cryptocurrencies or companies considering creating a market place for users to exchange cryptocurrencies must be aware and seek advice as to whether securities laws apply.

Hundreds of millions of dollars has been raised through ICOs. Startups create a new cryptocurrency that can be purchased with cash or an established cryptocurrency like bitcoin. The offering is often made over the internet and millions of dollars is transferred in a matter of minutes.

Investors hope that the value of their new coins will trade at higher values in either the ecosystem (or market) created by the ICO or their exchange value appreciates against other forms of cryptocurrencies and, eventually, can be exchanged for old fashioned fiat currency.

The offering does not give investors a "share" of the company. The terms of the offering may even explicitly state that the coins have no "rights, uses, purpose, attributes, functionalities or features, expressed or implied" as was the case with EOS.IO, a blockchain software company, recent offering. The CSA, however, has made it clear that disclaimers like this are not determinative of whether securities law applies; they will evaluate substance over form after considering the totality of the offering.

The CSA has reviewed numerous ICOs and concluded that on the whole where an "investment contract" has been created between the ICO offeror and the investor, the coin constitutes a security and securities laws should apply.

In determining whether an investment contract has been entered, the CSA sets out a four pronged test:



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Does the ICO/ITO involve:

1. An investment of money
2. In a common enterprise
3. With the expectation of profit
4. To come significantly from the efforts of others

If the offering meets this test, the offeror must comply with securities laws. This means that in order to complete the offering, the offeror must meet the time consuming and expensive prospectus requirements or complete the ICO under a prospectus exemption (e.g. accredited investor exemption, Offering Memorandum or the recently added but rarely relied on crowdfunding exemption).

Under certain conditions, typical of ICOs, the offering company might also have to register as a dealer in securities or meet a dealer registration exemption.

The CSAs role is to protect the public and investors. ICO and ITOs present a new, relatively untested means to raise capital. Unregulated, these capital raising means could leave the public vulnerable to scams.

If you are considering raising money by offering some form of cryptocurrency or blockchain-based software, consult your legal counsel. They can assist you in determining whether the coin you are offering constitutes a security and what steps you need to take in order to complete the offering legally.

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